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REFORM OF AFDC QUALITY CONTROL

HEARING

BEFORE THE

SUBCOMMITTEE ON HUMAN RESOURCES

OF THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

MAY 8, 1989

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REFORM OF AFDC QUALITY CONTROL

MONDAY, MAY 8, 1989

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON HUMAN RESOURCES,
Washington, DC.

The subcommittee met, pursuant to call, at 1 p.m., in room B-318, Rayburn House Office Building, Hon. Thomas J. Downey (acting chairman of the subcommittee) presiding.

[The press release announcing the hearing follows:]

FOR IMMEDIATE RELEASE
WEDNESDAY, APRIL 19, 1989

PR #7
SUBCOMMITTEE ON HUMAN RESOURCES
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES
1102 LONGWORTH HOUSE OFFICE BLDG.
WASHINGTON, D.C. 20515
TELEPHONE: (202) 225-1721

THE HONORABLE THOMAS J. DOWNEY (D., N.Y.), ACTING CHAIRMAN, SUBCOMMITTEE ON HUMAN RESOURCES, COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES, ANNOUNCES A HEARING ON REFORM OF AFDC QUALITY CONTROL

The Honorable Thomas J. Downey, Acting Chairman, Subcommittee on Human Resources, Committee on Ways and Means, U.S. House of Representatives today announced a hearing on alternatives to reform the Aid to Families with Dependent Children (AFDC) quality-control system, including the proposal in the Reagan Administration's fiscal year 1990 budget. The hearing will be held on Monday, May 8, 1989, beginning at 1:00 p.m., in room B-318 Rayburn House Office Building.

In announcing the hearing, Chairman Downey said: "Once again Congress must face a problem that will not go away on its own: the failure of the AFDC quality control system. Last year, we postponed the day of reckoning until July 1, 1989. This year, we have an opportunity to resolve this problem and move on to more important matters. I hope this hearing will provide the basis for a quick and decisive solution to this nagging problem."

The Consolidated Omnibus Budget Reconciliation Act of 1985 (P.L. 99-272) established a moratorium on the collection of AFDC fiscal sanctions. The moratorium prohibits the Department of Health and Human Services from reducing AFDC payments to States with high payment-error rates. The Family Support Act of 1988 (P.L. 100-485) extended this moratorium until July 1, 1989.

On January 9, 1989, the Department of Health and Human Services released a detailed explanation of the Reagan Administration's fiscal year 1990 budget. In it, two legislative changes were proposed for a new AFDC quality-control system: replacement of the current three-percent threshold for calculating State liabilities with a three-tiered system, similar to that recently enacted for Food Stamps; and prospective collection of State liabilities, beginning with those incurred for 1990, as is currently done for Medicaid quality control liabilities. However, the proposal did not address the disallowances since fiscal year 1981 that have not been collected.

Under the Reagan Administration's three-tiered system, States with error rates below three percent would receive bonus incentive payments. States with error rates of three to approximately six percent would submit a plan to reduce erroneous payments, and those above approximately six percent would be penalized for the amount between their error rates and three percent. Based on this approach, it has been estimated that the States would be required to repay about $80 million per year.

At the hearing, testimony will be heard from public witnesses. The Subcommittee is interested in testimony on the Reagan Administration proposal and the following specific issues:

- How should Congress deal with the backlog of disallowances going back to fiscal year 1981?
- What is a reasonable threshold above which States should be forced to pay back misspent Federal funds? Should the official error rate be the lower extreme of a statistical confidence interval? Should standard errors be published?
- Should so-called technical errors, those that do not have a direct effect on erroneous payments, be counted as errors for the purpose of calculating disallowances?
- Should States appeal directly to the Departmental Appeals Board, instead of first to the Secretary of Health and Human Services? How much time should be allotted for an administrative decision on an appeal?

- o What factors should the Departmental Appeals Board consider in deciding an appeal? Should it consider statistical validity and reliability? Should it consider offsetting Federal savings from overspent AFDC funds, such as underspending on Food Stamps?

- o Should the system explicitly provide for judicial review of decisions made by the Departmental Appeals Board?

- o Should the Federal government charge interest on disallowances when their collection has been delayed by an appeal, if the appeal is lost?

- o Should prospective collection of potential disallowances be adopted? Should the Federal government pay interest if the State's error rate is overestimated under a prospective system?

- o Should States be required to collect data on underpayments and negative case actions as part of the quality control samples? Should they report regularly on underpayments and negative case actions?

DETAILS FOR SUBMISSION OF REQUESTS TO BE HEARD:

Individuals and organizations interested in presenting oral testimony before the Subcommittee must submit their requests to be heard [(202) 225-1721] no later than the close of business, Tuesday, May 2, 1989. The telephone request must be followed by a formal written request to Robert J. Leonard, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. The Subcommittee staff will notify by telephone those scheduled to appear as soon as possible after the filing deadline. Any questions concerning a scheduled appearance should be directed to the Subcommittee [(202) 225-1025].

It is urged that persons and organizations having a common position make every effort to designate one spokesperson to represent them in order for the Subcommittee to hear as many points of view as possible. Time for oral presentations will be strictly limited with the understanding that a more detailed statement may be included in the printed record of the hearing. **(See formatting requirements below.)** This process will afford more time for members to question witnesses. In addition, witnesses may be grouped as panelists with strict time limitations for each panelist.

In order to assure the most productive use of the limited amount of time available to question witnesses, all witnesses scheduled to appear are required to submit 100 copies of their prepared statements to the Subcommittee office, B-317 Rayburn House Office Building, at least 24 hours in advance of their scheduled appearance. Failure to comply with this requirement may result in the witness being denied the opportunity to testify in person.

WRITTEN STATEMENTS IN LIEU OF PERSONAL APPEARANCE:

Persons wishing to submit a written statement for the printed record of the hearing should submit at least six (6) copies of their statement by the close of business, Monday, May 22, 1989, to Robert J. Leonard, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing written statements wish to have their statements distributed to the press and interested public, they may deliver 100 additional copies for this purpose to the Subcommittee office on the day of the hearing.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All statements and any accompanying exhibits for printing must be typed in single space on legal-size paper and may not exceed a total of 10 pages.
2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.
3. Statements must contain the name and capacity in which the witness will appear or, for written comments, the name and capacity of the person submitting the statement, as well as any clients or persons, or any organization for whom the witness appears or for whom the statement is submitted.
4. A supplemental sheet must accompany each statement listing the name, full address, a telephone number where the witness or the designated representative may be reached and a topical outline or summary of the comments and recommendations in the full statement. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press and public during the course of a public hearing, may be submitted in other forms.

Acting Chairman DOWNEY. The subcommittee will come to order.

This afternoon, the subcommittee returns to what seems to be a perennial issue—the failed quality control system under the Aid to Families and Dependent Children Program. This system is so strange, I am tempted to welcome you to the "Twilight Zone," but the topic is too serious for that. Although we must deal with such arcane concepts as standard deviations and confidence intervals, we must remember that the bottom line is providing cash assistance to needy children and their parents.

Last year, Congress extended the moratorium on collecting alleged misspent funds from the States through June 30, 1989. Presently, the Department of Health and Human Services estimates total potential disallowances from fiscal years 1981 through 1986 at about $1.2 billion. If Congress allows the moratorium to expire, the administration has projected that it would collect from the States $2.6 billion over the next 5 years. Before anyone jumps to the conclusion that his State is unaffected, let me tell you that all States, except Nevada, are subject to the sanctions.

Last year I said, "When an entire class flunks a test, the problem may not be the students. It could be the test, or it could be the teacher." Based on the testimony this subcommittee received last year on studies by the National Academy of Sciences and HHS, I have concluded that the test is unfair and the teacher has been blaming the students. We need to revamp the test so that the students know what to expect, and we need to give the students more feedback on how they can improve.

Let's get on with it.

Any of my colleagues wish to be heard on this scintillating subject?

Yes, Mrs. Johnson.

Mrs. JOHNSON. I want to say I welcome the various panelists as well.

This is a problem that has plagued us for a long time and simply needs to be straightened out so everybody at the Federal and at the State level knows what they are responsible for.

Thank you.

Mr. MATSUI. Mr. Chairman, I would only like to take this opportunity to thank you for holding these hearings. I know you participated in them last year as well. As you know, and you may have said in your opening remarks, the total amount allegedly due and payable now to the 49 States, technically out of compliance, is about $1.2 billion. This number is getting so out of hand it is almost impossible for the States to even consider paying it. So we do have to come up with a solution this time, one that will be binding on the House, the Senate, and the administration, and one that will allow the States to go ahead and make the plans in the future.

So I want to thank you for these hearings.

Acting Chairman DOWNEY. Thank you, Bob.

The subcommittee will now hear from Mr. Coyne. Bill, do you want to say anything?

Mr. COYNE. No.

Acting Chairman DOWNEY. We will hear now from Catherine Bertini, who is a native New Yorker from Cortland. Welcome to the subcommittee.

STATEMENT OF CATHERINE BERTINI, ACTING ASSISTANT SECRETARY FOR FAMILY SUPPORT, U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES, ACCOMPANIED BY MACK STORRS, ACTING DIRECTOR, OFFICE OF FAMILY ASSISTANCE

Ms. BERTINI. Thank you, Mr. Chairman. Thank you for inviting me to address this subcommittee on a topic of concern to the States, the taxpayer, and AFDC families: the quality control system for the AFDC Program. I must say at the outset we couldn't agree more we would like to come to some conclusion that we all can support and deal with in order to proceed with a system that we can all live with.

Before I begin, I would like to ask two things, Mr. Chairman. One, I would like to introduce Mack Storrs, the Acting Director of the Office of Family Assistance, whom I have asked to join me in the event you get into extremely technical questions.

Acting Chairman DOWNEY. Unlikely, but welcome.

Ms. BERTINI. And secondly, I would like my full comments to be included for the record.

Acting Chairman DOWNEY. Without objection, they will all be in the record.

Ms. BERTINI. Thank you.

In the past it seems that quality control has sometimes turned State governments and the Department of Health and Human Services into a situation like the Hatfields and the McCoys. As a result, Secretary Sullivan, taking the lead from President Bush, has made it clear that Government officials should work cooperatively and constructively to resolve this problem and other pressing problems. They also believe our national character can be measured by how we best care for our children, how we invest in them, how they grow, and the values and commitment we convey to them.

In the spirit of cooperation and commitment to those children, the administration today outlines a legislative proposal we hope will serve as an olive branch to the States and will begin our discussion towards a system that we can all accommodate.

At first glance, Federal quality control policies appear to have been an unqualified success. We have seen significant reductions in the level of error rates. National AFDC payment error rates fell from 16.5 percent in 1973 to 6.3 percent in 1987. The decreased error rates have allowed the States and the Federal Government to avoid billions in erroneous expenditures. State and Federal officials can take pride in these accomplishments and credit for substantially improved accuracy in AFDC benefits.

Unfortunately, it is a preoccupation with fiscal liabilities which make it impossible to continue these successes. Most States have repeatedly failed to meet the error standards that Congress has set. Many State officials allege the quality control requirements are too demanding and have asked the Congress for relief. This discord injects uncertainty and cynicism into the operation of the program. In view of these circumstances, the 99th Congress, as you mentioned, directed the Secretary to conduct a study and to contract with the National Academy of Sciences to conduct a study of how

to improve the effectiveness of the quality control system. As you mentioned, a moratorium also was put in place.

The Bush administration made use of the Academy's and the Department's reports in developing an improved plan for AFDC quality control. We believe the crux of the controversy revolves around the critical issue of what is a fair threshold for fiscal liabilities. It is the main focus for our change. Therefore, the Secretary will shortly send to Congress proposed legislation to create a new three-tiered system of incentives and liabilities similar in concept to the recently enacted revisions to the food stamp quality control system.

This proposal accommodates States' concerns by raising the error threshold and provides rewards for good performance. This plan also calls for inquiries into ways we can make the system more beneficial to needy families. The Secretary hopes this reform will bring the moratorium era to a close and permit all levels of welfare administration to concentrate on payment accuracy.

The plan would establish three tiers. In the first tier, States with error rates below an incentive target of 3 percent would receive an incentive payment equal to 50 percent of the Federal savings between 3 percent and the actual payment error rate.

In the second tier, States with error rates between the incentive target and a new threshold rate would be required to submit a comprehensive error reduction plan.

In the third tier, the Federal Government would not match erroneous payments in excess of the threshold rate. The States also would submit an error reduction plan. The threshold would initially be set at 6 percent but would be reduced one-tenth of a percentage point per year until fiscal year 1995, when the threshold would be fixed at 5.5 percent.

This path sets a reasonable phased improvement in lowering Federal and State costs for erroneous payments. Under the current system, as the chairman mentioned, 48 States are liable for $295 million in potential disallowances in fiscal year 1987. Under our proposal, less than 20 States would be liable for an estimated $80 million in fiscal year 1990.

Our decision to provide incentives follows the recommendations and the reports of both the Academy and the Department. The combination of bonus payments and disallowances reflects a more balanced approach to the AFDC quality control program.

Unfortunately, the current retrospective process for recovering disallowances only after prolonged appeal reduces the incentive for fiscal responsibility and program integrity. The Department has consequently decided to recommend a prospective method of collecting disallowances similar to that enacted by Congress in TEFRA for the Medicaid program. We propose that AFDC grants to the States be adjusted for estimated liabilities at the beginning of each quarter of the fiscal year. Error rates would be projected based on estimates established by the Secretary, taking into consideration past error rates. After the actual payment error rate for the year is established, the amount prospectively withheld would be adjusted accordingly. By insuring the timely recovery of erroneous payments, the new process will take into account the time value of money.

In conclusion, members of the committee may recall that on Inauguration Day the President proffered his hand and pledged to work with the Congress. We have already seen instances where good faith efforts by both sides can produce constructive results. It is certainly the Secretary's hope that quality control will follow these precedents.

With the presentation of this proposal, a first step has been taken towards resolving the quality control impasse. We are now willing to take additional steps, including discussions with congressional staff and representatives of State governments about alternative proposals—those within the confines of all of our budget constraints—so we can end this controversy as quickly as possible.

Thank you.

[The statement of Ms. Bertini follows:]

STATEMENT BY THE

ACTING ASSISTANT SECRETARY

FOR FAMILY SUPPORT

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Mr. Chairman and Members of the Committee:

Thank you for inviting me to address this subcommittee on a topic of concern to States, the taxpayer, and AFDC families: the quality control system for the AFDC program.

Sometimes it seems that quality control has turned State governments and the Department into the Hatfields and the McCoys. Secretary Sullivan, however, has made it clear that government officials should work cooperatively and constructively to resolve pressing problems. He also believes that our national character can be measured by how we care for our children -- how we invest in them, how they grow, and the values and commitment we convey to them. In the spirit of cooperation and reinvestment in our needy children, the Bush Administration today outlines a legislative proposal that we hope will serve as an olive branch to the States.

At first glance, Federal quality control policies appear to have been an unqualified success. We have seen significant reductions in the level of error rates. National AFDC payment error rates fell from 16.5 percent in 1973 to 6.3 percent in 1987. The decreased error rates have allowed the States and the Federal government to avoid billions in erroneous expenditures. State and Federal officials can both take pride in these accomplishments and credit for substantially improved accuracy in AFDC benefits.

Unfortunately, the controversy over, and focus of attention on fiscal liabilities impedes the continuation of these successes. Most States have repeatedly failed to meet the error standards that the Congress initiated in 1980. Thus, many State officials allege that the quality control requirements are too demanding and have asked the Congress for relief. The discord injects uncertainty and cynicism into the operation of the quality control program. The 99th Congress therefore directed the Secretary to conduct a study and to contract with the National Academy of Sciences for an independent, concurrent report on how to improve the effectiveness of the quality control system.

There were significant differences in the study approach and, as a result, in the findings and conclusions of each report. The Department conducted research and assessed the adequacy of the quality control system against the purposes for which it was designed -- to identify and avoid errors, to promote payment accuracy, fiscal responsibility, and program integrity. The Academy went beyond the current payment accuracy focus to consider and recommend broad, new systems of "quality improvement".

The Academy's report criticized the current quality control system and concluded that it does not meet the objectives of fiscal accountability or management improvement. Within the narrower scope of payment accuracy, relatively few questions were raised on the technical merits of the system. A key difference in the reports reflects the Academy's desire to expand the focus and include all goals simultaneously in one comprehensive performance measurement system. Thus, they recommended separate and substantially different Federal and State systems which we believe would substantially increase costs.

The Department's report found that the current quality control system is sound and has proven effective in reducing erroneous payments. The concept of a uniform, national error threshold and shared fiscal responsibility for error is fair, even though there may be disagreement on the appropriate level of the error threshold. The current system, with a State review of a sample of cases followed by a Federal re-review of a subsample, is an efficient use of shared information. We believe the current statistical principles and methods are valid and produce reliable estimates of payment error rates. However, States question the reliability of these estimates and we believe a reduction in precision resulting from much smaller Federal-only samples could indeed subject the reliability to question. The focus on payment accuracy is also necessary and proper.

We believe expansion of the current, Federally-established, uniform system to include broader measures of quality, efficiency, and effectiveness, as suggested by the National Academy of Sciences, is unnecessary. A wide variety of State performance measurement and management information systems already exist. Individual States can best define the management information and performance measurement systems necessary to achieve program goals; additional regulatory requirements are not needed.

While fundamentally sound, improvements to the current quality control system would make it better. But, the Department is in complete agreement with the Academy's observation that: "The controversy that gave rise to the study is about money: who should pay -- and how much they should pay -- for payment inaccuracies to recipients of family assistance." We believe that the crux of the controversy and our main focus for change revolve around the critical issue of what is a fair threshold for fiscal liabilities.

Administration's Proposal

Therefore, we will outline an improvement plan for AFDC quality control which will make it easier for Federal and State officials to obtain the maximum benefit out of each dollar. The Secretary will shortly send to Congress proposed legislation to create a new, three-tiered system of incentives and liabilities. The concept of the three-tiered system is similar to the recently enacted revisions to the Food Stamp quality control system. This proposal accommodates States' concerns by raising the error threshold and provides rewards for good performance. This plan also calls for an inquiry into ways we can make the current system more beneficial to needy families. The Secretary hopes that this reform will bring the moratoria era to a close and permit all levels of welfare administration to concentrate on payment accuracy.

The Department proposes to bring States into a partnership effort in quality control by using both carrots and sticks. The plan would establish three tiers. In the first tier, States with error rates below an incentive target of three percent would receive an incentive payment equal to 50 percent of the Federal share of savings between three percent and their actual payment error rate. In the second tier, States with error rates between the incentive target and a new "threshold" rate would be required to submit a comprehensive error reduction plan. In the third tier, the Federal government would not match erroneous payments in excess of the "threshold" rate. The State would also submit an error reduction plan. The "threshold" would initially be set at six percent, but would be reduced one tenth of a percentage point per year until fiscal year 1995 when the "threshold" would be fixed at 5.5 percent.

This path sets a reasonable phased improvement in lowering

Federal and State costs for erroneous payments. Under the current system, 48 States were liable for $295 million in potential disallowances in fiscal year 1987 (an estimated $215 million in FY 90). Under this proposal, less than 20 States would be liable for an estimated $80 million in FY 90.

An appropriate threshold should reflect a policy decision of the Congress and the executive branch as to what are tolerable amounts of erroneous payments. Decision makers should evaluate the public interest, the cost/benefit of error reduction and recognition of the difficulty of preventing all error. Taking these factors into consideration, and given past and projected error rates for AFDC, the Department believes this new threshold will foster management improvement.

Our decision to provide incentives follows the recommendations in the reports of both the Academy and the Department. The combination of incentive payments and disallowances reflects a more balanced approach to the AFDC quality control program.

Under a carrot and stick approach, the stick must be as credible as the carrot is appetizing. Unfortunately, the current retrospective process for recovering disallowances only after prolonged appeals reduces the incentive for fiscal responsibility and program integrity. The Department has consequently decided to recommend a prospective method of collecting disallowances, similar to that enacted by the Congress in TEFRA for the Medicaid program. We propose that AFDC grants to the States be adjusted for estimated liabilities at the beginning of each quarter of the fiscal year. Error rates would be projected based on estimates established by the Secretary, taking into consideration past error rates. After the actual payment error rate for the year is established, the amount prospectively withheld would be adjusted accordingly. By insuring the timely recovery of erroneous payments, this new process will take into account the time value of money.

In the past, the limited, available data on so-called "negative case actions" have made it imprudent to use such actions for fiscal liabilities. In response to concerns that quality control treats AFDC families unfairly, the Department plans to study ways to hold States accountable for underpayments, improper denials, and incorrect terminations.

Currently, denials and terminations are sampled under a separate system which establishes a case error rate based on whether procedures were properly followed. The Department will conduct research on ways to develop reliable measures of the cost of improper denials and terminations. Based on the results, we will examine whether to impose fiscal liabilities for unacceptably high rates of underpayments, improper denials and terminations. We will advise Congress of these findings and our recommendations.

It is our hope that the completion of this study will bolster confidence in the Department's commitment to insuring that each AFDC family obtains the full level of benefits to which it is entitled.

Secretary Sullivan is also committed to assisting States to innovate and respond to changing circumstances. Quality improvement and error reduction require commitment to creative innovation--the process of developing, evaluating, and sharing new techniques and approaches. Within current authority and resources, we will strengthen our efforts in this area. Further, the Department will expand current activities associated with the identification of "best practices," the sharing and dissemination of these techniques and in facilitating the direct, hands-on transfer of technology from one State to another.

Conclusion

Members of the Committee may recall that on Inauguration Day the President proffered his hand and pledged to work with the Congress. We have already seen instances where good faith efforts produce constructive results. It is certainly the Administration's hope that quality control will follow these precedents.

With the presentation of this proposal, a first step has been taken towards the resolution of the future quality control system. We look forward to working with Congress toward enactment of this proposal.

Subcommittee Questions

At this point in time, I would like to respond to some of the specific concerns which were raised in the subcommittee's press release of April 19.

1. How should Congress deal with the backlog of disallowances going back to fiscal year 1981?

The Department, like the subcommittee, is concerned about how to address the backlog of disallowances. Full payment of all disallowances might present some States with budgetary difficulties. However, partial or complete forgiveness of these disallowances raises questions of equity. These disallowances were properly calculated using a sound system established under regulations required by statute. Is it fair to those States which took great pains to meet the error rate standards established by Congress to retroactively change the ground rules?

We believe discussion to resolve the backlog of disallowances should be kept separate from the institution of a future quality control system. Backlogged disallowances are primarily a budgetary concern, and should not be allowed to confuse and delay progress on developing an effective policy for the future.

2. What is a reasonable threshold above which States should be forced to pay back misspent Federal funds? Should the official error rate be the lower extreme of a statistical confidence interval? Should standard errors be published?

Clearly, the current legislated three percent rate is a rigorous standard for AFDC. Only six States achieved this rate for fiscal year 1987. One important consideration, however, is the extent to which the Federal government should match the erroneous payments. In recognition of recent Congressional and past State concerns and based on evaluations of State error reduction efforts over the years, we have proposed an increase in the error tolerance to six percent, which is the lowest national average payment error rate. Neither the Department nor the States should be satisfied with this level of achievement. Therefore, we have proposed modest annual reductions of one-tenth of a percentage point for five years to encourage improved payment accuracy.

The Department wishes to retain the current method of the statistical calculation of the error rates for three reasons. First, the point estimate is universally regarded by statisticians as the "best" estimate of the actual error rate. Second, since we use a regression methodology, the lower bound of the statistical confidence interval can be manipulated intentionally or affected inadvertently by an improper quality control review by States. This results in a wider confidence interval and an artificially lower error rate at the lower bound.

The Department believes that standard errors should be published. We published annual statistical analyses that included standard errors through 1985. We plan to resume the publication of standard errors in the future.

3. Should so-called "technical errors," those that do not have direct effect on erroneous payments, be counted as errors for the purpose of calculating disallowances?

We believe that so-called "technical errors" are within the control of the State. By definition, the agency can correct them. We are examining this issue.

The subcommittee should bear in mind that these errors can have an effect on payment. For example, if the State had documented a single Social Security number, a bank or wage match might have uncovered resources which would have impacted AFDC payments. Furthermore, the income verification requirement enacted in the Deficit Reduction Act of 1984 depends on accurate Social Security numbers for data matches to insure that applicants and recipients receive the amount of AFDC assistance for which they are entitled.

4. Should states appeal directly to the Departmental Appeals Board, instead of first to the Secretary of Health and Human Services? How much time should be allotted for an administrative decision on appeal?

With respect to the Departmental Appeals Board, States should and currently do appeal directly to the Departmental Appeals Board. The Department does not provide for an optional appeal to the Secretary. We believe the time for all appeals should be limited, since it is important that all issues are evaluated and resolved in a timely manner.

5. What factors should the Departmental Appeals Board consider in deciding an appeal? Should it consider statistical validity and reliability? Should it consider offsetting Federal savings from overspent AFDC funds, such as underspending on Food Stamps?

Currently, the scope of the Board's review of disallowances does not include the review of the validity of the regulations and the quality control waiver decision of the Department. The decision of the Secretary on waivers is a discretionary authority of the Secretary and as such is not subject to review by the Board. In all other instances the Board determines what issues are relevant based on its deliberation of an appeal request. We do not believe it would be appropriate to specify or limit the factors which should be considered by the Board.

Under current program appropriations, there is no authority for one Department to offset either the under or overspending of another Department's program. Therefore, it would not be appropriate for this Department's Appeal Board to consider offsetting Federal savings.

6. Should the system explicitly provide for judicial review of decisions made by the Departmental Appeals Board?

We are consulting with the Department of Justice on this question. One approach would be enactment of a judicial review statute related to Departmental Appeals Board decisions on only those cases involving question of law. The statute should specify the court of jurisdiction, the scope of the review should be limited to matters of law, and the time frame for requesting judicial review should be swift.

7. Should the Federal government charge interest on disallowances when their collection has been delayed by an

appeal, if the appeal is lost?

The Department currently allows a State two options when issuing disallowances: 1) reconcile the disallowance promptly to avoid assessment of interest or 2) retain disallowed funds while pursuing administrative appeals. If the latter outcome favors the Department, the State is liable for interest. This is congruous with the Executive Branch's responsibility to taxpayers to exercise proper cash management. Failure to collect interest on Federal dollars distributed to the States and then disallowed would ignore the time value of money.

Further, it seems illogical to presume that a losing plaintiff would expect special financial consideration from a defendant.

8. Should prospective collection of potential disallowances be adopted? Should the Federal government pay interest if the State's error rate is overestimated under a prospective system?

The Department seeks the establishment of prospective disallowances for two reasons. First, the current system in AFDC does not take into account the time value of money. Timely recovery of excess erroneous payments in the year in which they are incurred is a key to proper cash management.

Second, the use of a prospective payment system will restore some of the muscle in the disallowance system. Litigation and repeated moratoria have diminished the credibility of fiscal liabilities. State officials may not believe there is a need to improve their payments system when they know they will not be held accountable for years to come.

The Department therefore recommends that AFDC grants to the States be adjusted for estimated liabilities at the beginning of each quarter of the fiscal year. Error rates would be projected based on estimates established by the Secretary, taking into consideration past error rates. After the actual payment error rate is established, the amount prospectively withheld would be adjusted accordingly.

The Secretary is aware of warnings that prospective disallowances will shortchange state welfare programs. He will closely monitor the implementation of this new process to insure that it does not jeopardize the operation of public assistance systems.

The Department does not believe payment of interest is appropriate on either side, if the State's error rate is overestimated or underestimated and the adjustment is promptly made. The Department bears no legal or financial obligation to pay interest on Federal monies that it provides to or withholds from the States. The over or underestimation will be adjusted at the next fiscal quarter when the actual error rate is available.

9. Should States be required to collect data on underpayments and negative case actions as part of the quality control samples? Should they report regularly on underpayments and negative case actions?

The Department maintains that any action to hold States accountable must include all errors. Quality control should demonstrate a balanced interest in all payment accuracy errors.

The Department plans an evaluation of the feasibility, methodology, and resource requirements of an expanded negative case action system for determining payment error rates before they are used for fiscal liability purposes. The Food and Nutrition Service is conducting similar research under contract

in the quality control negative case action system of the Food Stamp program. We are reviewing the materials developed by their contractor with the view of perhaps adapting them and testing them for use in our program.

The Department wishes to note that an historical comparison of overpayment and underpayment error rates does not indicate that the current disallowance policy has resulted in increased rates of underpayment. Generally, as States have reduced the overpayment error rates, underpayments have declined as well.

The Department has not recommended immediate sanctions for negative case actions because of the technical difficulties involved in such an effort. An individual, whose application was denied or whose assistance was terminated, no longer has any relationship with the welfare agency. The validity of calculating a payment error rate for negative case actions may be dependent on how many of these individuals we are able to track down and how well they cooperate.

I would be happy to respond to any additional questions you may have.

Acting Chairman DOWNEY. Thank you, Ms. Bertini.

I am going to inform the members that we are going to operate under the 5-minute rule and all the panelists to come will also be operating under the 5-minute rule.

Ms. Bertini, in your testimony, you stated the backlog is primarily a budget issue and it should be resolved separately from any reform of the system.

How do you propose to resolve this backlog? Would you favor forgiving any of it?

Ms. BERTINI. We think, Mr. Chairman, there should be two separate discussions, one about how the system should operate in the future, and that is the proposal we have on the table. We don't think we should mix the two discussions. There should be a separate discussion about what we do about the backlog. The backlog discussion has additional parameters given the fact that future budgets include the assumption of collecting these erroneous dollars and so they would add additional budget constraint to the discussion as well.

Acting Chairman DOWNEY. I had a discussion with OMB Director Darman when he came before the committee and I suggested that the chances of our collecting this backlog any time soon were slim to nonexistent. I asked him if he had put it in his budget, and he had. With a twinkling of the eye, he told me that they anticipated that they would collect this revenue, but one got the feeling, though it certainly was not said, that it was more of a fond hope than anything else.

Let me ask you a couple of questions. I think that is a constructive approach, and I would like you to think about some of the ideas that we have batted around here. In the process, if we are not going to collect this money, perhaps we should require the States, possibly based on the amount that we forfeit, to reinvest in reducing their errors. This would require that they make some additional expenditures on their own. I would hope you would keep an open mind to that, because I think it would be a salutary outcome. As I read this proposal, it looks remarkably like the Reagan administration proposal. Is that correct? Could you point out some of the differences between these proposals and the Reagan proposal?

Ms. BERTINI. It was developed during the last 2 months, so there is kind of a carryover between the Reagan proposal and the Bush proposal. However, it is a new proposal that we have not put on the table before. It is new for us.

Acting Chairman DOWNEY. The Hunger Prevention Act of 1988 revamped the food stamp QC program. Congress determined that a 5-percent error rate threshold was too low for assessing penalties, and instead, passed a threshold equal to the lowest national average ever achieved plus 1 percent, or the current year's national average, whichever was lower.

According to the data that we have, that would set the food stamp threshold at 7.6 percent for fiscal year 1987. Could you support a similar threshold to that, and if not, could you then explain to us why you chose 5.5 percent?

Ms. BERTINI. Let me back into that and answer the second question first. We started with 6 percent because that was the lowest national error rate achieved by States for fiscal year 1984. They ac-

tually reached 6 percent. So, in an effort not to be arbitrary in coming up with a number, we knew that 6 percent was an achievable and realistic goal.

Also, in an effort to not only start with an achievable goal, but also to put in some downward trend of those numbers in order to continue to encourage States to watch this carefully, we thought it made sense to promote continued improvements. We came down over 5 years to 5.5 percent. That is how we came up with those numbers.

Now, to answer your first question, the difference, of course, between 6 percent and 7 percent, or whatever it would be, is a number that we then have to plug into the budgetary figures to consider its impact.

Now, Senator Moynihan's proposal goes the other way, of course, and says that we would use the last year's rate minus 1 percent.

Acting Chairman DOWNEY. I understand that both Medicaid and food stamps don't count certain procedural errors in the official error rates and that explains why there is in Medicaid, for instance, a 2.9 percent error rate in 1984. Why would procedural errors that we agreed have no effect on the payments, count in AFDC program when they are not counted in food stamps and Medicaid?

Ms. BERTINI. A couple of reasons. One, there is a statutory reason why Medicaid does not count the so-called technical errors. Congress passed legislation prohibiting them from counting it. That is why they didn't.

The Department has taken the position that we are supposed to use all the eligibility factors, given the fact Congress has said these are the eligibility factors. In Medicaid, Congress specifically said, don't use them in calculating State error rates and didn't say it to AFDC. We concluded that we are required to count them.

Food stamps operates differently. They just decided they won't count them—the so-called technical errors. The reason why we maintain we should count them are as No. 1, it is statutory direction. And No. 2, although some of them don't directly affect payments, some of them could.

The one, I think, that is different than the others is the Social Security number, because there may be some connection, some use of the Social Security number to verify, for instance, other income or bank accounts or resources.

The other point that I think is important to keep in mind in dealing with the technical error issue is that if we substracted them, for instance, from the 1987 totals, we still won't get to the level of Medicaid. We would go from about 6.3 to about 5, 5.1, something like that.

Acting Chairman DOWNEY. As a matter of policy, to have one program for food stamps, another for Medicaid, and another for AFDC doesn't make a great deal of sense in terms of administrative ease. Is that a reasonable point?

Ms. BERTINI. Yes, certainly to the extent we do have in all three programs very many of the same functions, it would probably be easier for States to accommodate that.

Acting Chairman DOWNEY. Let's assume we didn't do anything and the moratorium expired this summer. How quickly do you think you would be able to collect the sanctions?

Ms. BERTINI. I would probably have to give the same answer that Director Darman did, or you gave yourself. It certainly will be in litigation for a while, I would expect.

By the way, I also should point out that in the Family Support Act we were given direction to proceed with the process, which means that we would reissue the fiscal year 1981 disallowance letters and the States would be given an opportunity to appeal back to the Departmental Appeals Board to begin the process. We believe you all directed us to do that.

Acting Chairman DOWNEY. All right. We look forward to working with you on this. I really don't want to put this off another year if we don't have to. Mr. Frenzel and Mr. Gradison, who are no longer members of this subcommittee, felt strongly we should not have put it off last time. I was inclined to agree with them, but we were not then in a position to deal with it.

This year we should try our mightiest to fix it and fix it in time for reconciliation.

Mr. Matsui.

Mr. MATSUI. Thank you, Mr. Chairman.

I think you are right, Ms. Bertini, in trying to divide the issues. One obviously has to deal with the backlog and how we are going to deal with this issue in the future.

I appreciated the fact you did look to the National Academy of Science study because that is a definitive study, one we can work and build off of.

In your proposed legislation you have taken into consideration overpayments. Now, would a State be sanctioned if they made underpayments as well? You have to have both sides of the coin in order for this to work. Otherwise, they would be more apt to be conservative and not make payments that perhaps legitimately should be made.

Would you put both those sides of the coin in your proposal?

Ms. BERTINI. They aren't in our current proposal; the underpayments, including nonpayments to denied or terminated individuals, are not. We agree with you, Congressman, that it is very important to try to deal with the underpayment issue.

We have not been able to get our arms around it for a couple of reasons. One of them is because it is difficult to pinpoint, particularly if someone has not gone on the rolls or is off the rolls, exactly what happened in the process. In our proposal, we recommend that we do—I hate to say further research in an effort to say we are putting it off, but it is very important that we do some further research to be able to figure out exactly what we can do.

The current system, of course, only deals with overpayment errors. Since underpayments are payments not made, they would be handled perhaps differently. But we do appreciate the importance of this issue. The last thing we want to do is to deny a client who deserves to receive AFDC benefits and we want to figure out a way to be able to do that.

Mr. MATSUI. The Academy does suggest you do it both ways. I am concerned about the beneficiary.

I am more concerned that you have both an underpayment/overpayment approach because that is the only way you keep the system honest. Otherwise, as I indicated, people would be apt to make underpayments rather than overpayments because they would be sanctioned.

But if they would be sanctioned on both of them they would probably be more apt to be accurate than to play either way. You know, in your testimony and in your public comments you indicate that the rules should be changed. I think everybody acknowledges that.

I don't know of anybody who would say that they like the status quo. Is that my understanding?

Ms. BERTINI. Yes, sir.

Mr. MATSUI. That being the case, I don't know how we can really then separate the two issues completely. I think there has to be some kind of linkage between what we want to do prospectively, current law, and the fact we do have these enormous back payments.

I was just looking over the back payments for some of our colleagues and, as you well know, in the State of California it is $247 million. In Connecticut and their small population, it is $4.6 million. In New York, it is substantial.

In Pennsylvania, it is substantial. It is substantial in almost every State that has AFDC payments. If we acknowledge the fact that the former approach was erroneous and we have to make changes, then it is very difficult to say that the States should be penalized under a system that we acknowledge today is flawed. I would like your comment on that.

Ms. BERTINI. Two issues. One, we don't think the system now is flawed. We think it is a contentious issue because there is such a problem with collecting the backlog now, that we really do need to accommodate a system where we really can ensure that the money that is misspent is collected. So, in fact, in coming up with a proposal for making a suggestion for the future—this is why I said they should be split issues—we are trying to deal with the future. One other issue that relates to the backlog is that the States who were able, though be it a small number of States, to get under 3 percent or the States that end up with a very small disallowance and we are particularly diligent in getting to that point, may be penalized by going backwards now.

Mr. MATSUI. I will tell you what the problem is, though. Those small States you are talking about are States like Nevada, States that don't have much in terms of AFDC benefits.

If they have no program, of course they are not going to be penalized. We only have 5 minutes so I am not going to be able to get into the premise you made, the success or the fact you feel the current law is adequate.

First of all, I think in your opening statement you mentioned that from 1973 to 1987 the error rate was 16 percent in the former and 6.3 percent in the latter. That very well may be. In fact, we all acknowledge that but over the last 4 years since we have been working on this program, testimony has come out to indicate from 1973, that is when the AFDC Program essentially started, the States had a very difficult time putting their programs together

and, as a result of that, you would expect larger error rates in the early years of a new program.

As the States became more sophisticated, as they learned more, as they gained more expertise through their own case workers and administrators, the error rate went down. So I wouldn't necessarily say it was the Michel amendment that resulted in a 10-percent drop in the error rate.

I think the States had an incentive to drop the error rate. That is why I really question the whole issue of why anybody would say that old program was successful. I am really surprised you would say it is an adequate program.

The AFDC–QC system didn't take into consideration, for example, the recession of 1982, 1983 and 1984, when all of a sudden you saw enormous increases in case loads in States in the Midwest, Michigan, Minnesota, States that had the auto industry in it.

It was a test that was based only numerically, and it didn't take into consideration clerical errors and those kinds of things.

Could you just comment on that?

Ms. BERTINI. Sure. Those are concerns I know you have, Congressman, particularly that you had last year as well. Our statistical data show that there could be as many as 38 different factors that affect the error rate one way or another.

But to specifically take out one or two would not give an adequate view of the whole process.

Acting Chairman DOWNEY. Mrs. Johnson.

Mrs. JOHNSON. Thank you very much.

I think it is significant that since 1980 most States have repeatedly failed to comply. Under your new formula, 20 of the 48 States would have reduced their liability dramatically. Does that mean that the other 28 States would have no liability under the new formula?

Ms. BERTINI. Yes, it does mean that for one of two reasons. Either they would have been under the 3-percent threshold, in which case they, in our proposal, would get an incentive, or they would be between 3 and 6 percent, in which case they would have no financial liability but they would have to put together a plan, corrective action plan in order to try to lower their error rates.

Mrs. JOHNSON. So your plan does at least cut the problem slightly more than in half?

Ms. BERTINI. Yes.

Mrs. JOHNSON. I have a problem with creating a national level that would automatically float as a function of State error rates. It seems to me that rewards error rates.

So I want you to spend 5 minutes talking a little bit more about the error rates.

What does cause them? Why is it States have had such great difficulty in complying? When you talk about clerical errors, surely we don't want to reward States for clerical errors.

What kind of clerical errors? I know we are going to hear some testimony from the States about this, but I would like to hear your analysis of the two or three factors that cause the greatest problem and that your scheme would eliminate.

Ms. BERTINI. OK. I would be glad to. For starters, the error rate problem, everyone I think agrees we ought to look at the States

that have large error rates. The question is, where is the line to be drawn in the process?

But if we look at the error rate process, it is a combination of the States and the Federal Government reviewing the AFDC caseload. The States take a sample. It is almost like taking a political survey in terms of finding a statistical sample of cases to pull out, although the formula is obviously much different, but that is the concept.

The States take a sample and they look at the sample to see whether or not they have misspent money, did they decide in this case of this particular woman and her children that the State actually paid them the amount of money they are supposed to get. Then the Federal Government takes a subsample of the State sample. The State's error rate is calculated using the results of both samples.

One of the technical errors, or clerical errors, that you referred to is WIN registration.

Since clients are supposed to register for participation in WIN, if they did not, that would be found in error, even though that may not have affected how much money was the correct payment to that individual.

That type of error is going to disappear because WIN registration is no longer going to be a part of AFDC after the Family Support Act is implemented. So that piece will go away.

Another reason is the Social Security numbers that I mentioned. Social Security numbers are required for obvious reasons, to be able to double-check against a person's claim. We believe that those, for instance, are significant to the process because cases without a Social Security number are more difficult cases in which to verify income and resources.

If a recipient in the monthly reporting system fails to file a monthly report, an ineligibility technical error is cited regardless of whether the recipient is otherwise eligible.

Monthly reporting is a congressionally mandated piece of our program. That sometimes causes an error. All technical errors are a little more than 1 percent of the total. So if we took, for instance, a 6.3-percent error rate from 1987, the technical errors were 1.15.

Mrs. JOHNSON. So they are small.

Ms. BERTINI. They are small in number. Now, they end up being about one-third of the total disallowance because if you take the 3-percent target, subtracted from the 6——

Mrs. JOHNSON. What are the major problems in the other sectors?

Ms. BERTINI. With the errors in general?

Mrs. JOHNSON. Yes.

Ms. BERTINI I am going to get Mack Storrs to give you some background on that.

Mr. STORRS. I think one of the problems in the whole thing is the program is very complex, and errors result from changing circumstances so people have earned income and their circumstances are changing. It is hard for eligibility workers who have high, heavy caseloads to keep track of all changes. Often clients fail to report on changes. Either they are unaware of or they consciously do not report those changing circumstances.

It is a complex program where basically every dollar of income needs to be accounted for or every dollar of resources needs to be accounted for. So any change in a client's circumstance has an effect, and clearly there are a number of factors. We identified 38 different variables in our study of what are the causal factors that affect error rates. But they affect the error rates differently in different States. Some States have been able to adjust to it, and some have not.

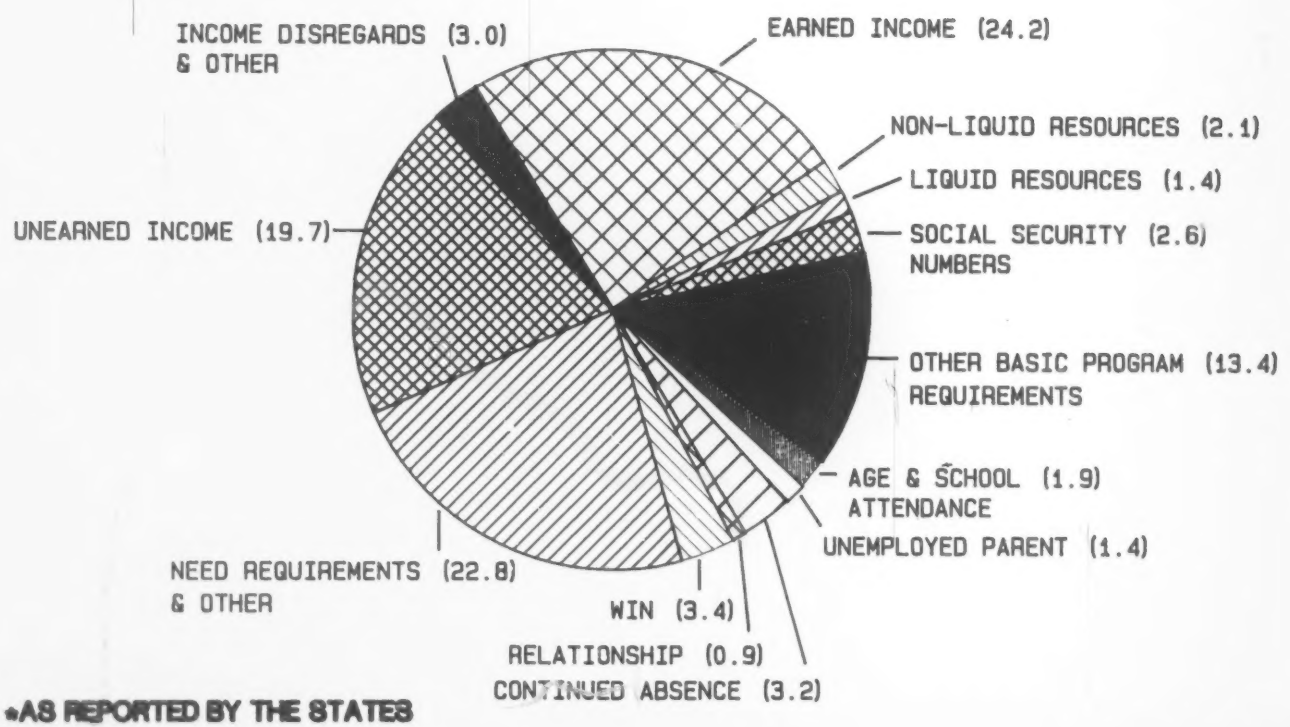
Ms. BERTINI. If I may make one other comment, we can provide you a breakdown, specifying the breakdown, for instance, of the 1987 error rates and exactly what percent was unearned income, which was about 20 percent, income disregards, earned income and others. We have a listing which we can provide to you if you would like.

Mrs. JOHNSON. I think, Mr. Chairman, if that was provided for the record, that would be helpful as well.

[The information follows:]

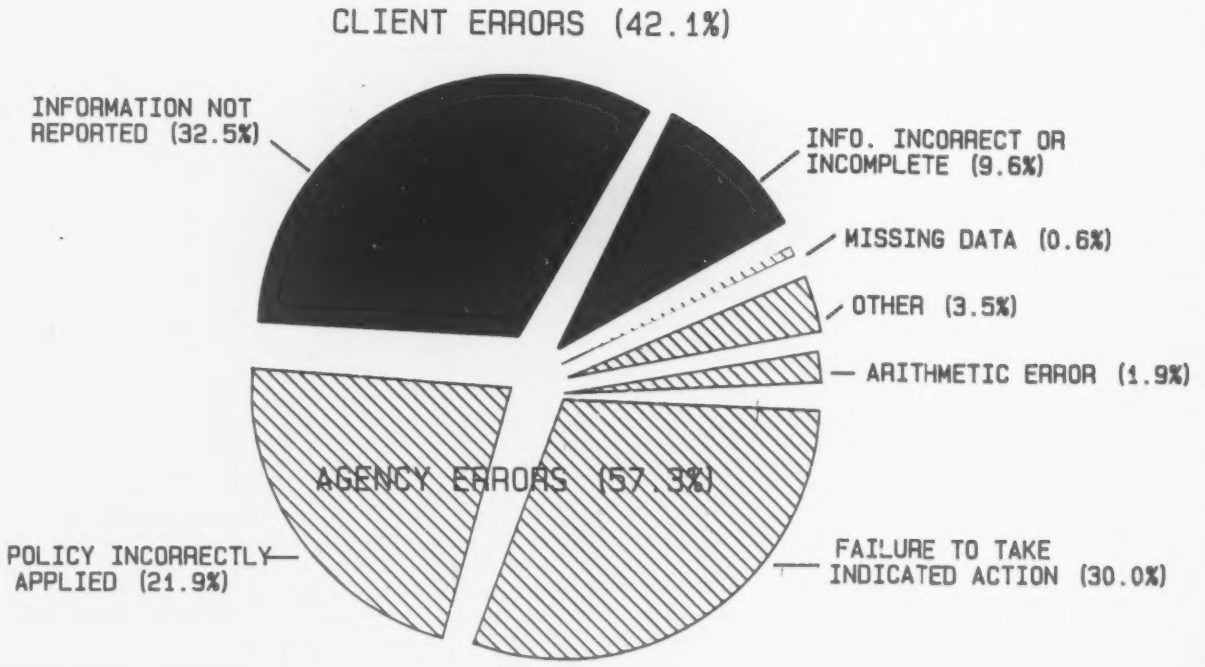
FY 1987 — WHERE PRIMARY TYPE OF AFDC PAYMENT ERRORS ARE FOUND*

Percent of Total Error Payments



*AS REPORTED BY THE STATES

PERCENT OF TOTAL AFDC ERROR CASES ATTRIBUTED TO THE AGENCY OR THE CLIENT, * FISCAL YEAR 1987



*AS REPORTED BY STATES

Acting Chairman DOWNEY. Mr. Coyne.

Mr. COYNE. I have no questions, Mr. Chairman.

Acting Chairman DOWNEY. Mr. Shaw.

Mr. SHAW. I think, Mr. Chairman, that nearly all the questions have been asked. I would just like to join you in welcoming Ms. Bertini to the committee. It was a nice surprise to see you here this afternoon. I think I met you about 10 years ago when I was mayor of Fort Lauderdale, and it is very nice to see you again.

Ms. BERTINI. Yes, sir. In fact, my brother is one of your constituents.

Mr. SHAW. I was just telling Mr. Downey about you. Your brother used to play a trumpet in the band at Fort Lauderdale and was in the circus for a while.

Acting Chairman DOWNEY. Is he also a Cortland native?

Ms. BERTINI. Absolutely. Cortland High School.

Acting Chairman DOWNEY. Mr. Ford, do you have any questions?

Mr. FORD. No, Mr. Chairman. I would like to thank HHS for coming over to testify, and since Mr. Shaw is fortunate to have your brother in his district and you go to school with the chairman, I was wondering if you know anybody in the Memphis area.

Acting Chairman DOWNEY. The subcommittee will next hear from its first panel. Gregory Coler, secretary, Florida Department of Health and Rehabilitative Services; Bob Greenstein, executive director, Center on Budget and Policy Priorities; Charles A. Miller, Covington & Burling; and Alicia Smith, director, Committee on Human Resources, National Governors' Association.

We will begin with Mr. Coler.

STATEMENT OF GREGORY L. COLER, SECRETARY, FLORIDA DEPARTMENT OF HEALTH AND REHABILITATIVE SERVICES AND CHAIRMAN, ECONOMIC SECURITY COMMITTEE, NATIONAL COUNCIL OF STATE HUMAN SERVICE ADMINISTRATORS, AMERICAN PUBLIC WELFARE ASSOCIATION

Mr. COLER. Thank you very much, Mr. Chairman. I appreciate the opportunity to testify before you today.

I would like to summarize the points in my testimony, Mr. Chairman, if I might, and submit the entire testimony for the record.

Acting Chairman DOWNEY. Please do.

Mr. COLER. I think one of the most important points that you just heard about was the reason given in response to Congresswoman Johnson's question about why States have error rates. As we pursue the goals of the Family Support Act, we are going to be facing a great disincentive to achieve those goals because the cases, as you just heard from the testimony from HHS, that are most complex, that cause the States to have errors, are those where there is income. Obviously, the point of the Family Support Act, which all of us who administer these programs at the State level are very grateful to you Mr. Chairman, Congressman Matsui and the other congressional leaders, who saw to it we now have a Federal law that provides tremendous incentives and really reforms, for the first time, our whole approach to welfare in the United States.

So now we have this wrong-headed, mean-spirited quality control system that we have been battling with for years; sort of a wolf which we are never sure whether it is going to bite us or not. Now we have new goals you have set for us. You have told us to get into a new business, to be efficient and effective employment agencies for people on welfare. We are coming to the task, my colleagues and I, with great vigor, with tremendous enthusiasm to achieve those goals.

But as we do, as we bring people from welfare into a state of independence through helping them to get jobs and retain those jobs, those are going to be the cases where we will have errors, because the current quality control system makes these cases extremely error prone. The point Mack Storrs made is important, both because monthly reporting administrative errors are counted the same as eligibility errors and because the current system of retrospective budgeting leads to an enormous volume of income changes for clients to report and for staff to process.

In Florida over the last 2 years, as we have implemented Project Independence, we have doubled the number of people placed in jobs as a result of our efforts. We expect that production to accelerate as we take advantage of the tremendous benefits that you have provided for us in the Family Support Act. Our original State legislation only provided for 3 months of transitional day care and Medicaid. Now we will have a year. Obviously, it will be a lot easier for us to achieve our goal of self sufficiency.

I wanted to point out one of the most important reasons State welfare administrators think H.R. 2243 is so important and so overdue, is because quality control currently does present a disincentive to charge ahead with the very admirable goals of the Family Support Act.

I say the system is wrong-headed and mean spirited because how can a system be described otherwise where you count over-payments but you don't count under-payments? Certainly in any system that is fair, we ought to be as concerned about those who don't get the money as those that we over-pay. It harkens back to the old debate where we don't like welfare, because we don't agree with the goals of the program. All the old stereotypical statements about welfare come up, since we weren't too sure what to do and it took us 30 years to get to the Family Support Act, maybe some people even go back before H.R. 1 and long, before that.

But because it took us so long, the quality control system continues to be one of those systems that just punishes, doesn't provide any rewards or incentives and is very very arbitrary. Why 3 percent? Why 6 percent? Why 8 percent for a national tolerance level?

The National Academy of Sciences has defined without equivocation that the system makes no sense from any statistical approach to how you develop a fair quality control system. As you pointed out in your opening remarks, 49 States are now sanctioned to the tune of some $1.2 billion. The figure will increase to $2½ billion by next year. Obviously something needs to be done now to resolve it.

Whether the State's error rate was affected by factors beyond the State's control, such as caseload growth, caseload composition, program changes, strikes or natural disasters, all are an important part of Congressman Matsui's bill. I wanted to point out to Con-

gressman Shaw, in Florida a good example of this was evident when we had the Mariel boatlift, USDA gave us a waiver on the errors made. We couldn't get the same waiver for AFDC, costing Florida $5.5 million.

Again, you have this inconsistency, with one part of the Federal definition of poverty imposing one set of sanctions and relief and the other part being completely inconsistent. But that is the type of error that Florida had as a very special exception that, in my mind, reflects the wisdom of the particular criteria in House bill 2243.

Whether the error rate is statistically reliable is certainly something that the National Academy of Sciences has pointed out needs to be examined. Some type of national average, some type of reasonable approach that gives us a clear view of what good effort towards administering the program is and isn't, I think, is a very laudable goal for the bill.

APWA's National Council of State Public Welfare Administrators has a fundamental statement on quality control, and I would like to submit it as a part of the record. The four principal criteria in that statement are a reformed system should separate management and audit functions, State progress and error reduction must be considered, States should only be penalized for actual misspent dollars, and a system that penalizes the poorest performing States should also reward those States that have the best programs all should be built into the legislation.

We believe that interest payments on sanctions doesn't make a lot of sense, not unless the Federal Government would reciprocate and have the title IV-E money, some $700 million that is owed the States, be paid with interest, and we don't think that makes a lot of sense. But just from an equitable standpoint, I would offer that as a reason why there should be no interest.

We strongly oppose prospective collections. It would impose, in our mind, a double penalty on the States, a penalty we think is already not a very fair one, and we just think you should carefully consider, as we believe you are, a reasonable threshold. The current thresholds are not now scientifically grounded and do not relate to the actual or potential capability of individual States. We are not advocating that the national tolerance level be eliminated. We are asking it be realistic and related to the national average, like most curves are and most things we grade, and then measure ourselves against it. It should also be reviewed periodically to addressing changing circumstances.

These Federal regulations we deal with would confound a rocket scientist. They change continuously. They are extremely complex. I challenge any of you to do a work day. Go to your State welfare department, and say "I want to learn how you fill out one of these eligibility forms." I guarantee you if your congressional seat depended upon your doing it at a 3 percent error rate within 48 hours of training, you would have spent some long long nights in your office. It is that tough. Our staffs change continuously. It is very hard to, if not impossible, to meet the 3-percent error rate.

The thing you have done to help us the most is give us 90 percent reimbursement for family assistance management information systems, FAMIS. Any State like Florida, which is currently in the

green eye shade and quill pen stage where we are making do with pencils on scratch pads, will never be able to reduce error rates the way we have in Medicaid, where we already have an automated system.

We have now committed ourselves to have such a FAMIS system. We have completed the advanced planning document and received approval. We have done the procurement. We have gone through all the steps. We are going to sign the contract. We will overhaul Florida's entire approach and automate it hopefully within the next 30 months. That is what the contract calls for. Half the States have those systems up and running today.

Whatever you can do to further encourage the rest of the States to automate, will drive down the error rate. Because obviously computers are going to do those calculations at less of an error rate and at less expense than human manpower could, and we could use the human manpower to help convince people to leave welfare.

I would suggest that automation is a very positive step that could be looked at by the committee, because it truly is one thing that will bring us better management results.

Thank you.

Acting Chairman DOWNEY. Thank you.

[The statement of Gregory L. Coler follows:]

TESTIMONY OF GREGORY L. COLER, SECRETARY
FLORIDA DEPARTMENT OF HEALTH AND REHABILITATIVE SERVICES
Representing the
NATIONAL COUNCIL OF STATE HUMAN SERVICE ADMINISTRATORS OF THE AMERICAN PUBLIC WELFARE ASSOCIATION.

Mr. Chairman, members of the Subcommittee, my name is Gregory Coler and I am the Secretary of the Florida Department of Health and Rehabilitative Services. I am here today as Chairman of the Economic Security Committee of the National Council of State Human Service Administrators of the American Public Welfare Association (APWA). APWA is a 59-year-old nonprofit bipartisian organization representing the 50 state human service departments, 800 local public welfare agencies and 6,000 individuals nationwide. APWA advocates sound, effective and compassionate social welfare policy at the national, state, and local levels, and brings state policy leadership into national decision-making, as demonstrated during the 100th Congress in debate on the Family Support Act of 1988.

It is a particular pleasure for me to appear before this committee today. It is a privilege to be able to commend each member for your dogged determination, particularly Chairman Downey, in pursuing reform of our welfare system. The Family Support Act represents an opportunity for thousands of Americans to escape dependency and achieve self-sufficiency. My fellow commissioners and I are committed to making this laudable goal a practical, tangible reality.

I also want to commend this Committee for its long and exemplary record on the issue of quality control reform. The committee's leadership, and particularly the contributions of Mr. Matsui and Chairman Downey, are appreciated and supported by state human service administrators across the country.

The Current Quality Control System

Let me focus on the reason for this important hearing, how best to improve the current quality control system as it relates to AFDC. Let me make clear from the outset that state welfare administrators, no less than the federal government, strongly believe in the concept of a national quality control system. Proof of our commitment is clear in the substantial reduction of state error rates in AFDC over the last decade.

How did the states do it? Through the commitment of top management time and energy to error reduction. We have dedicated new resources to error reduction by, lowering caseloads, streamlining paperwork and increasing systems automation. States have worked well with each other to exchange ideas on error reduction. I assure you that our progress has not occurred because the threat of stiff federal sanctions has prodded us into better performance. We have state legislators, governors, the media and the voters to provide the necessary encouragement. States have as much at stake as the federal government - they pay a large share of the cost of welfare programs, and in some states, more than half the bill. State administrators care about payment accuracy and support performance accountability for the needs tested entitlement programs they administer. Our primary goal remains the effective and compassionate delivery of services to eligible low-income families in order to promote their self-sufficiency.

Today the quality control system is not functioning as the management tool it was intended to be. Instead, the QC system in place today focuses all its resources into the assessment of only one indicator of quality in our programs: payment accuracy. Our programs have many other important results that can be measured on performance--such as job placements, child support enforcement collections, and timely action on applications. And we must find time and resources to hold ourselves accountable in these areas. As the QC system now operates, it stands out as one of the most forbidding obstacles to good management and to efforts to move America's poor into self-sufficiency. It diverts the efforts of managers from real results and if continued, siphons off millions of dollars intended for programs for the poor.

The National Academy of Sciences (NAS) substantiated the concerns of many members of this Committee and human service commissioners last year in its report on the QC system by recommending a restructuring of the current performance assessment mechanisms by separating management and audit functions. NAS stated that a sound quality control system should set sanctions and records so that only states at the extremes of good or bad performance are subject to rewards or sanctions. Under our current QC system forty-nine states face quality control sanctions, totaling $1.2 billion in the AFDC program for fiscal years 1981-86. In my own state of Florida, we estimate our total sanction liability at $22.1 million for FY 81-86 and we are estimating an additional liability of $20 million for FY 87 and FY 88, with much of that due to highly technical errors that do not have a direct effect on erroneous payments.

Time for Reform is Now

In 1987, Florida began a major welfare-to-work initiative that we call Project Independence. In the time since its implementation, we have substantially increased the placements of AFDC clients in jobs. In the state fiscal year prior to Project Independence we achieved 12,500 AFDC placements. In the first full year of Project Independence we nearly doubled that figure, making over 22,000 AFDC placements. We expect to reach close to 25,000 AFDC placements in the current state fiscal year.

The Family Support Act mirrors the thrust of our own welfare reform program. It is exactly this type of innovative solution to a difficult problem that can be stifled by the structure of the current QC system. The threat of severe sanctions tends to distort management decisions by forcing states to focus excessively on payment accuracy, often to the exclusion of other critical agency outputs and goals.

New programs are too often judged by whether they will affect the error rate rather than by their potential for finding jobs for recipients or helping improve child support collections. Even worse, there is evidence that in the desperate pursuit of unreasonably low federal error rate targets, some states are imposing new eligibility verification requirements that have the unintended effect of blocking or delaying payments to families legally eligible for assistance.

As the system now operates, erroneous denials do not count toward sanctions, but erroneous payments do. The current system also creates disincentives for collecting useful information by concentrating nearly all of it resources on narrow technical issues, rather than taking a more comprehensive look at whether the program is working. A less rigorous scrutiny will lead to fewer errors and thus come closer to meeting federal error rate targets, but will not necessarily tell you if the program is working.

Today the most compelling reason to reform the QC system is that it now diverts needed resources from real error reduction efforts and other initiatives. When my fellow commissioners and I go to our governors and our legislators, as we recently did in order to implement the provisions of the Family Support Act, there is a limited pot of money available. If we have to pay large amounts for unreasonable sanctions, that money will not come from a state tax increase, or from the transportation budget. It will come either from administrative budgets, which pay for our staffs and computers, or from a prospective AFDC cost-of-living increase, a new job training program, or a shelter for the homeless.

Florida is making rapid progress finalizing the procurement for a computer system that will give us the technical capacity to perform these functions on-line rather than on paper. Until that system is implemented, however, states like Florida, whose systems rely on paper and pencil transactions to produce grant

changes, are severely impacted by a QC system that makes every change in a client's situation an opportunity for error. The irony here is that if our staff and computer fall victim to budget cuts because of unfounded sanction penalties, our error rate will go up, not down.

Now I will turn to two of the most difficult questions facing you as you consider reform of the quality control system for AFDC: what to do with the backlog of sanctions and how to create a rational performance assessment system with a reasonable national threshold. I will also discuss two points the Administration has shown an interest in, prospective collections and interest on sanctions. My colleague Patty Day will discuss technical questions in greater detail from her perspective as a quality control administrator.

The Backlog of Sanctions

One of the most pressing problems facing all of you as Members of the 101st Congress is how to reduce the federal deficit. The $1.2 billion in past sanctions, if they are collected, certainly would be a tempting solution to part of the problem. The expectation you may have of collecting these sanctions was recently addressed in report language accompanying the House Budget Committee's First Concurrent Budget Resolution, and I quote,

> The Committee assumptions do not project collections of fiscal penalties from states under the QC system in AFDC for either FY 1989 or FY 90. The issue of QC sanctions is subject to appeal by the states to the Department of Health and Human Services (HHS) Grant Appeals Board and possible judicial challenge. It is also likely that the Congress will address the QC sanctions issue in future legislation. The assumed collection of fiscal penalties from states in FY 91 and beyond are based on current law. Because of the potential for appeals, judicial challenge, and legislative changes, the 1991 and 1992 collection assumptions are subject to a great deal of uncertainty. It is possible that the current law assumptions may overstate actual future collections.

APWA believes there is a better way to resolve the backlog problem than through endless rounds of negotiations and appeals to HHS and years of litigation. We believe that legislation developed by this committee should authorize the HHS Departmental Appeals Board to examine the case of each state that does not qualify for an exclusion from sanctions as is the case in legislation introduced by Senator Moynihan (S. 231). The Appeals Board should have the authority to determine whether sanctions are warranted for these states and the appropriate sanction amount. These determinations should be based on an inquiry of whether, and to what extent, a state's QC record reflects a pattern of actual, avoidable misspending of federal dollars. The inquiry should follow the standard used by the NAS: states should be held accountable only for rules that were known in advance and for procedures over which they have control. The relevant factors to be considered by the Board should include:

- Whether the state's error rate is sufficiently statistically reliable for a conclusion that the state exceeded the tolerance level or whether the state's penalty is upwardly biased;

- Whether the errors for which the state was cited in fact represent net misspending of benefit funds. In Florida, removing technical errors and considering underpayments in computing the error rates would result in a savings to the state of $1.6 million for FY 81-86 and over $9 million for FY 87 and 88.

- Whether the error rate was affected by factors beyond the state's control, such as caseload growth, caseload composition, program changes, strikes or natural disasters; Again citing my own state, the rapid influx of refugees, particularly those who came to Florida as part of the Mariel boatlift, were accepted in a waiver request to the Department of Agriculture as an exceptional circumstance. USDA agreed not to sanction the state for the impact on the food stamp error rate, saving the state some $5.4 million in FY 81. Yet, HHS did not accept this same event as an exceptional circumstance that impacted on our AFDC error rate and refused to grant a waiver for the $3.5 million HHS contended the Department owed as a result of this uncontrollable circumstance.

- Whether the state's record with respect to corrective action demonstrates a reasonable concerted effort to reduce errors; and

- Whether the state's error rate history is consistent with the error rate for the period in question.

This proposal would help protect states against unwarranted sanctions for past years. At the same time, the proposal creates an opportunity to enact QC reform with a modest impact on federal deficit calculations. Inclusion of this approach in QC reform legislation in the House would provide a means whereby some sanctions could be collected in FY 1990, a year for which the Congressional Budget Office and the House Budget Committee now estimate no collections. Therefore, this solution to the backlog of sanctions issue would make it possible to enact QC improvements legislation this year as a deficit-neutral or even deficit-reducing measure.

Reasonable Threshold

The National Academy of Sciences' study states, "current thresholds are not now scientifically grounded and do not relate to the actual or potential capability of individual states." The Academy then went on to point out, "there is something wrong with a system that still finds nearly all of the operational units doing poorly in the face of their record of improved national performance." Only two states have consistently met the national target for the period of 1981-86.

Despite the considerable investment made by the states to reduce errors, only one state has been able to achieve the 3% standard for more than a year and a half and less than 10% of the states have been able to maintain an error rate below 4% for the same length of time.

Clearly, 3% is an unrealistic standard given the complexity of the AFDC program. As one of the most complex endeavors of the public sector, AFDC is inherently prone to some level of error. Eligibility workers must examine a myriad of factors to determine eligibility and benefits under severe time constraints. Federal quality control reviewers, on the other hand, review only a small percentage of AFDC cases over a much more extended period of time and with the benefit of the results of the state's own quality control review. In effect, states are penalized for failing in their regular determinations to perform at the level achieved by federal reviewers operating without time constraints.

The reasonableness of the current 3% tolerance, given state experience, the effort that has already been made in corrective action, and the NAS findings, clearly point out the need for revisions in the determination of a national tolerance level. I want to assure this committee that my fellow commissioners and I will continue to strive for lower errors regardless of the national tolerance level. Our large financial stake in the program requires us to do so. If the national tolerance level is

enacted into law as introduced by Congressman Matsui (H.R. 2243), Florida would save an estimated $15 million, enough to pay the salaries of all eligibility workers and their supervisors in Ft. Lauderdale and Miami for one year.

As long as the federal government chooses to impose fiscal sanctions based on quality control performance, it is critical that reasonable and accurate standards are set. We are not advocating that a national tolerance level be eliminated. We ask that it be realistic. Given the findings of the Academy, APWA contends that the target should be related to the national average. This is a fairer and more representative tolerance based on current potential. We also recommend that the national tolerance level be reviewed periodically. This is consistent with the NAS recommendation that the national tolerance level should be modified to address changing circumstances, such as the refugee influx in Florida.

Prospective Collection

APWA strongly opposes the prospective collection of potential disallowances. States know from their experience with the program that error rates alone are not sufficient indicators on which to base fiscal sanctions. The potential for problems exists even if the QC system is reformed. Prospective collection would impose a double penalty on states for their most recent error rates--thus taking resources away from states, which they may need for corrective action. Prospective collections also ignore potential improvements in program operation by states from year to year.

Interest on Sanctions

APWA opposes paying interest on sanction dollars for two very specific reasons. One is the obvious point that has been stated throughout this testimony that the statistical validity of the current QC system is very much in question in the minds of virtually everyone who has looked closely at the system. The other point has to do with money that is owed states for programs like foster care. IV-E back claims owed to the states now exceed $700 million and no one has suggested that states receive interest on those back claims. Equity demands that neither the states nor the federal government should consider interest payments a part of the reimbursement procedures in these programs.

Conclusion

I would again like to commend the leadership that this committee has exhibited on an issue that is not easy or attention grabbing, yet is critical to the delivery of needed services to low-income Americans. The 50 state human service commissioners stand ready to work with you to develop a reform package that includes a rational and fair system of fiscal accountability for AFDC and the other programs we administer. In the Family Support Act you told those of us who operate AFDC program to emphasize employment and child support to help welfare clients attain self-sufficiency. We are asking you to give us a QC system that encourages our effort, not one that penalizes us, and through us the families and children we serve.

Thank you for the opportunity to present our views. I would be happy to answer any questions you might have.

APWA

NATIONAL COUNCIL OF STATE HUMAN SERVICE ADMINISTRATORS

NCSHSA Policy Statement on

QUALITY CONTROL AND PERFORMANCE ACCOUNTABILITY

Preface

Congress has called into question the validity of the current quality control processes. The National Academy of Sciences has substantiated these concerns and recommends restructuring the current performance assessment mechanisms used in the AFDC, Medicaid and Food Stamp Programs. State administrators in accordance with the changes recommended by the National Academy of Sciences urge Congress to put in place a fair and equitable system for assessing state performance. Current sanction policies threaten the integrity of the major entitlement programs, and inhibit future innovation in the administration of these programs.

Quality Control Studies

Numerous studies criticizing the current quality control systems have been conducted over the last decade. In a series of studies the General Accounting Office has faulted many aspects of the current system, particularly, the bias in using the mid-point of the confidence interval in a penalty system.

The most comprehensive study of quality control to date is the congressionally mandated study of quality control in the AFDC, Medicaid and Food Stamp Programs by the National Academy of Sciences. The National Academy reaffirms earlier findings, calls for comprehensive reform and urges the separation of management and audit functions in the quality control system. The Academy's recommendations for change are consistent with the principles for reform adopted by state administrators.

The Academy praises state efforts and progress in reducing mispayments and recommends a reformed system that holds the federal agencies and states mutually accountable for program performance. The Academy, like state administrators, believes states should not be penalized for factors they cannot control.

Background

The states strongly support performance accountability for needs-tested entitlement programs administered by the states and jointly funded by federal and state appropriations. For states the primary goal in administering the AFDC, Medicaid and food stamp programs is effective and compassionate delivery of services to eligible low income families. States urge the Congress to put in place a fair and equitable system to assess state performance and encourage, rather than inhibit, management improvements. Such a system must address the need for coordination of policies, particularly quality control policies, in all three programs. There must be a mutual obligation on the part of the states and the federal government to better serve eligible persons.

States and localities as well as the federal government have a major financial interest in proper administration of these programs. Each error in the AFDC and Medicaid programs costs states dollars that states can ill afford to expend as they seek to accomplish program objectives. States are as concerned as federal officials that benefits be targeted toward those who need them most. Payments to ineligible persons and overpayments are an unacceptable waste of both state and federal resources. At the same time, reducing improper denials and underpayments must also be a priority for state and federal agencies.

As evidence of our commitment to reducing errors, the states have accomplished significant reductions in error rates over the past several years. Since the early 1970's, the AFDC program error rate dropped from 16.5 percent to 7.1 percent; the food stamp program error rate dropped from 16.0 to 7.6 percent; and the Medicaid program error rate dropped from 6.2 to 2.3 percent. In all three programs the greatest error reduction was achieved prior to the imposition of fiscal penalties in 1981. This reduction in error rates was achieved in spite of increasing complexities in federal regulations. States believe that further reductions in the mispayment error rate can be achieved, but only if the federal policies, regulations, and initiatives reflect a cooperative relationship that seeks to effectively reduce program inconsistencies and complexities.

State administrators therefore urge Congress to develop nationwide standards of achievable performance thresholds which equitably and reasonably acknowledge caseload characteristic and demographic differences. Further, we believe that disincentives for excessive failures need to be balanced with incentives.

State administrators are committed to reducing mispayments and curtailing the unacceptable waste of state and federal resources. Whether this will be achieved will depend on Congressional action to revise the current processes.

Current Sanctions

Under the current quality control systems, the states face AFDC sanctions totaling more than $1 billion over the next few years. Moreover, it appears that sanctions in the Food Stamp and Medicaid Programs will equal close to $500 million over the same period of time. These sanctions are an inflated, inaccurate representation of actual misspent dollars. Should such punitive sanctions be imposed, these consequences are clear:

- The resulting shift of costs from federal to state governments will have an immediate and significant impact on the ability of the states to finance human service programs which may result in the reduction of services to those most in need;
- States will be forced to increase administrative expenditures with little or no evidence that such expenditures will be cost-effective;
- Pending sanctions threaten the very error reduction efforts Congress envisioned. Further, the current sanction systems distort management priorities by forcing an exclusive focus on payment accuracy.

Principles for Reform

State administrators strongly support reform of the quality control system in the AFDC and Medicaid programs. States also support additional reform of the Food Stamp quality control system. A fair and equitable quality control system must be based on the following principles:

- Both federal and state government are responsible for administration of the AFDC, Medicaid and Food Stamp Programs. Therefore, both must be held accountable for efficient management of these programs.

- Given that the current quality control processes serve primarily federal interests, a reformed system must separate the management and audit functions.

- State performance should be assessed according to the federal/state agreement on program administration represented in the state plan. Any discrepancies between state and federal agencies over a state plan or program manuals should be dealt with in the compliance process.

- The states' progress in error reduction must be considered. The standards to which states are held accountable should be based on demonstrated state achievement not arbitrary standards.

- A system that penalizes the poorest performing states should also reward those states who are the best performers.

- States should only be penalized for actual misspent dollars. Technical errors should not be tied to fiscal penalties and state penalties should be reduced by overpayments recovered.

- States should not be penalized for errors based on information unavailable at the time of the state review, yet available at the time of the federal review.

- Acceptable measures of performance should be based on statistical estimates designed to shift the margin of error in the states favor, i.e. use of the lower bound of the confidence interval in lieu of the point estimate in calculating payment accuracy rates. In addition a fair measure of performance must take into consideration significant demographic and program variations within and across the states.

- States with a financial liability should have the opportunity to reinvest in activities designed to reduce erroneous payments. Similarly, a fair and effective mechanism should be available to provide administrative relief for such states.

- For its part, the federal government should be held accountable for reviewing the reported quality control findings in a consistent and timely manner. More flexibility is needed to enable both the federal government and the states to compensate for inaccurate federal data (e.g., BENDEX, IEVS data).

- Federal support is needed to minimize the impact of federal programs and policy changes on state performance. Special attention must be given to simplifying and coordinating the three diverse federal programs. Given program complexity, states should be afforded adequate lead time to implement federal program changes and should not be subject to sanction during the implementation of new policies.

Acting Chairman DOWNEY. Bob.

STATEMENT OF ROBERT GREENSTEIN, DIRECTOR, CENTER ON BUDGET AND POLICY PRIORITIES

Mr. GREENSTEIN. Mr. Chairman, I appreciate the opportunity to be here today.

I am Robert Greenstein, director of the Center on Budget and Policy Priorities, a nonprofit organization that conducts research and analysis on Federal and State programs and policies that affect low-income families. In 1979 and 1980, as Administrator of the Food and Nutrition Service at the U.S. Department of Agriculture, the agency that runs the Food Stamp Program, I was responsible for design and implementation of the original food stamp error rate sanction system. In 1982, after establishment of the center, I helped design and draft, at the request of Senator Robert Dole, a Dole amendment establishing the food stamp error rate sanction system in effect from 1983 through last year.

I was involved in the negotiations in last year's Hunger Act that helped reform the system. I am probably the only person in this room right now who is a Federal official who actually imposed and collected fiscal sanctions from States during my tenure in the Federal Government.

As you noted, Mr. Chairman, in your opening statement, unless one concludes nearly every State in the Nation is nearly deficient in operating its program, one has to conclude the error rate standards is unrealistic. Certainly, the conclusion the National Academy of Sciences came to when it recommended a revamped system that identifies state agencies that are unusual because of extremely good or bad performance, levies sanctions or confers rewards on them but not the others, it is the same situation we were in in food stamps prior to last year, and I think it is why that system was reformed on a bipartisan basis.

Indeed, the existence and the renewal of the moratorium is itself a clear reflection of the political untenability of the current system, as well as its substantive deficiencies. Rather than attempting to sanction 45 to 50 States, collect virtually none of the sanctions, and face inevitable congressional action if the mountain of back sanctions ever really becomes due, we need a system that targets and isolates the States that are the serious offenders and secures either large-scale operational changes in those States that will save millions in the future or actually collects the sanctions in question.

I am hopeful we are actually at the point where we can disabuse ourselves of the notion that ever larger sanctions translate into ever lower error rates. They do not. To the contrary, the experience of recent years demonstrates there is a point beyond which imposing increased sanction liabilities on more States can actually be counter-productive. The Reagan administration recognized that last year and joined with the Congress and others of us in overhauling the food stamp system in a bipartisan manner in a way that reduced the number of States subject to sanctions to about 10, with total potential sanction liability of about $40 million a year.

Indeed, I would urge the subcommittee to look carefully at the structure of the new food stamp sanction system. I note that the Acting Assistant Secretary just mentioned that as a model in describing the new administration proposal. I would have to say, however, while the new proposal is described as a significant advance in some respects, in other respects it actually is quite different from the food stamp proposal enacted last year.

In the new food stamp error rate sanction system, the concept is used of levying sanction liabilities on States whose error rates exceed the lowest national average achieved, and this has the advantage of tying the threshold, it is done in a way if the national average goes down, your sanction goes down. If the national average in a given year floats back up, your threshold does not go back up because it is the lowest national average achieved. I believe it should probably be the lowest national average achieved prior to the year in question so that States know the target before the year starts, they have a clear goal, and that is what they have to shoot at.

The system has one other important element there, and that is it notes the fact that as in political polling, State error rates are not precise. They are based on a small sample that is projected to the whole caseload. The truer rate may be higher or lower than the official rate figure. It often is—at least the margin of error is often at least 1 percentage point on either side of the State's error rate.

For that reason, the new food stamp system sets the sanction level the national error rate plus 1 percentage point. That is done for a very good reason. It is to insure that a State does not get sanctioned if it is truer or the rate is below the national average.

It was mentioned earlier by the Acting Assistant Secretary that the Moynihan bill—and I think the Matsui bill as well—set the threshold as national average minus 1 percentage point. We need to be careful not to confuse apples and oranges here, the Moynihan bill and the Matsui bill use the lower end of the confidence interval, that drops you down about 1 percentage point, and then use the national average minus 1 percentage point, that is one approach.

I think the national food stamp approach is simpler and more equitable, which is to use the mid points rather than the lower point of the confidence interval because that interval varies from State to State.

One more point on this. The food stamp threshold, therefore, for the current year would not be 7.6; it would be 8.6.

The second area in which the new proposal of the administration would be different than the food stamp system—and I think the food stamp system is superior—is in the question of underpayments. Right now we have an unbalanced system that effectively says to States when in doubt, reduce or deny benefits. Our message to the States should be clear. The goal is accuracy. Families should get neither more nor less than they are entitled to.

The food stamp system deals with this by taking each State's overpayment and underpayment rate and adding them together. The total is then compared to the sum of the national average overpayment and underpayment rates plus the 1 percentage point. If you are over that, you are sanctioned.

The Assistant Secretary mentioned that a study was needed on this. Again, I think we need to be careful here. It is true that we do not know now and do not have the data to derive a dollar amount for improper denials and terminations. We do have the data we need to get a dollar rate for underpayments to eligible households, that is in the food stamp sanction system now. It was in as far back as 1980 and 1981. We do not need further study to get that information, and there really I think is no equitable basis for not including that in a sanction system unless you need to say that underpayments are OK whereas overpayments are not.

I would be particularly concerned with a system that rewards States that have low overpayments without any regard to how high their underpayment or improper denial rate is. In 9 years of food stamp sanctions, we have never had a system like that there. I am concerned that is part of the new proposal here. I think it is quite important that be even-handed.

The final major area I want to address, and again where the new proposal differs from food stamp practice, regards a point you raised about technical errors. I would strongly urge the subcommittee to reform the current rules of AFDC regarding technical errors. The current AFDC rules in this area conflict with food stamps and Medicaid.

More important, they have no sound analytical basis. Technical errors are those errors that, if corrected, have no effect on the amount of benefits paid. They thus differ sharply from errors that, if corrected, would result in a different benefit level. Failure to report income, for example, is a nontechnical error. If you knew the household's income, it failed to report it, benefit would go down.

On the other hand, if a quality control review finds a monthly report form is missing from a case file but the family's income is proper in the case file, the family size is proper, the benefit level is right, no overpayment has occurred; but under the current system the entire payment to the household is considered to be an overpayment.

The Acting Assistant Secretary said it was important to count technical errors such as Social Security numbers, because if not handled properly they could lead to error. True enough, wrong conclusion. If lack of a Social Security number or a lack of a monthly report led to an improper benefit level, QC picks up the improper benefit level. That is an overpayment. That is recorded as an overpayment.

What inclusion of technical errors means is the following: It means in those circumstances in which lack of a social security number of a missing form from a file makes no difference and the benefit was right anyway, you count it as an overpayment. Because if the benefit is wrong, you already catch it through the regular QC system.

This same argument was made to the National Academy of Sciences by the then HHS Assistant Secretary. It was rejected not only interestingly by the Academy, which found that position unsupportable, but it was rejected in the major study of the food stamp quality control system conducted under the Reagan administration and issued by the U.S. Department of Agriculture in 1987.

The Agriculture Department said it as well as anybody. They said procedural deficiencies, such as a missing signature on an application, lack of a work registration card, or lack of information on Social Security numbers, do not necessarily lead to an incorrect benefit. Such errors could indirectly lead to issuance of errors since they might be indicative of other problems, but if this is the case, the QC system will capture these errors where they matter, when benefits are incorrect. Correcting the procedural error itself would not alter the eligibility or benefits of the household. Excluding purely procedural errors is consistent with measuring the rate of erroneous overissuance.

What we now do is the following. We sanction a State and ask them to pay back the Federal Government for technical errors that did not result in any loss of Federal funds, and then we go to the recipient, and we make the recipient pay back an overissuance that the recipient did not in fact receive. I think this is as egregious as any part of the system. It has never been, as far back as I can remember, a part of food stamps, and when I was administering the program, I asked my counterpart in about 1980 at HHS why there was a similar provision in AFDC. And the answer I was given was it was basically indefensible but HHS at that point was afraid the Congress would criticize them if they removed technical errors from the error rate framework.

Mr. Chairman, the final point I would like to make is there is one other area where the administration's proposal would differ from the new food stamp proposal and that is the prospective collection of error rate sanctions. I think that question gets to the heart of the matter of what is your goal.

Is the Congress' goal to reduce, to improve management, and reduce errors in the future or is your goal to get a bunch of money from the States and put it in the Federal Treasury?

Whichever you decide leads you in a different direction.

My own experience leads me to think that the proper goal ought to be improved management and reduced errors in the future.

When I was at the Agriculture Department, we targeted the five States that were costing the Federal Government the most money through high error rates.

We threatened to impose substantial sanctions on all of them. We had specific milestones for corrective actions and as the States took them, in some cases we actually forgave the sanctions.

The result was that in every State, the error rates came down dramatically.

The Federal Government saved tens of millions of dollars over subsequent years. When you move instead to a system that is automatic—you are above a threshold, you automatically collect it—in fact, don't wait until the State is above the threshold assume they will be and collect it in advance.

You do two things. One, you remove money from the State on front end invested to improve management.

Two, you lose the Federal Government's leverage to creatively use the threat of a sanction to leverage management improvement you might not otherwise get. I think that is probably not the proper way to go.

So, in conclusion, I think that last year's Hunger Prevention Act offers a very interesting model, but I would look at it carefully and I think it differs in a number of key respects from the proposal we heard earlier here this afternoon.

Thank you.

Acting Chairman DOWNEY. Thank you.

[The statement follows:]

TESTIMONY OF ROBERT GREENSTEIN
DIRECTOR OF THE CENTER ON BUDGET AND POLICY PRIORITIES
before the
SUBCOMMITTEE ON HUMAN RESOURCES
HOUSE COMMITTEE ON WAYS AND MEANS

May 8, 1989

I appreciate the opportunity to appear before the Subcommittee today. I am Robert Greenstein, director of the Center on Budget and Policy Priorities, a non-profit organization that conducts research and analysis on federal and state programs and policies that affect low income families. The areas of quality control and error rate sanctions are areas with which I have been involved for some time. In 1979 and 1980, as Administrator of the Food and Nutrition Service at the U.S. Department of Agriculture (the agency that runs the food stamp program), I was responsible for design and implementation of the original food stamp error rate sanction system. In 1982, after establishment of the Center, I helped design and draft (at the request of Senator Robert Dole) a Dole amendment establishing the food stamp error rate sanction system in effect from 1983 through last year. From 1985 to 1987, I and other Center staff prepared a series of four analyses of various issues related to quality control and error rate sanction systems, and last year we were involved in the negotiations that led to enactment of bipartisan legislation overhauling the food stamp sanction system. In addition, as the federal official responsible for the food stamp program in the late 1970s, one of my principal charges was to reduce food stamp error rates and to threaten to use and actually use fiscal sanctions as a tool to help secure this result.

The AFDC Sanction System: A System that Does Not Work

The AFDC sanction system today is much like the food stamp system was prior to its overhaul by Congress last year -- a system that does not work very well. One of the most serious flaws in the system is that it fails to distinguish poorly performing states from other states. Like the old food stamp sanction system, the AFDC system subjects nearly all states (more than 40) to sanction liabilities every year. A system that sanctions nearly all states is usually a system that is inadequately designed from a substantive standpoint -- and a system that generally will not work from a political standpoint.

On the substantive side, unless one concludes that nearly every state is seriously deficient in operating its program, one must conclude that an error rate standard which results in nearly all states being subject to fiscal penalties is unrealistic. The National Academy of Sciences panel observed in one of its reports on quality control systems:

> The panel concludes that there is something wrong with a QC system that "finds" nearly all of the operational units are performing poorly . . . Either the standards of performance are too tight, or the QC system has failed to put in place the mechanisms that could achieve those standards in that period of time.

The NAS panel recommended that a revamped system should "identify state agencies that are unusual because their performance is extremely good or extremely poor" and levy sanctions (or confer rewards) on these states but not on others.

On the political side, when 40 to 50 states are subject to sanctions each year, the sanctions will be largely unenforceable and are likely never to be collected. When sanctions grow too large and are spread over too many states, the states band together to devote major resources to fighting them in Congress and in the courts, and federal officials delay or back off from sanction collections. When sanctions are too massive and too widespread, they become like a nuclear weapon -- the impact is so overpowering that you can't actually use them. What you get instead are moratoria on sanction collections.

Indeed, the existence and repeated renewals of the moratoria are a clear reflection of the political untenability of the current sanction system, as well as of its substantive deficiencies. Rather than attempting to sanction 45 states, collect virtually

none of the sanctions, and face inevitable Congressional action if the mountain of back sanctions ever really becomes due, we need a system that targets and isolates the states which are the serious offenders and either secures very large-scale operational changes in these states that will save millions of dollars in the future or actually collects the sanctions in question.

In short, we need to disabuse ourselves of the notion that ever larger sanctions translate into ever lower error rates. To the contrary, the experience of recent years demonstrates that there is a point beyond which imposing increased sanction liabilities on more states can be counterproductive.

I believe a recognition of these realities is what led to a reversal of the Reagan Administration's position last year, when the food stamp system was overhauled in a manner that reduced the number of states potentially subject to sanctions from approximately 45 to about 10, with total potential sanction liabilities of about $40 million a year.

Where to Go From Here?

As noted, the National Academy of Sciences panel recommended that the sanction system identify and target the states whose error rate performance has differed significantly from the norm. This is an eminently sensible recommendation. The new food stamp system, by focusing on about 10 states, moves in this direction.

The structure of the new food stamp system warrants careful examination by the Subcommittee. I should note that while the proposal in the final Reagan budget is sometimes described as being patterned on the new food stamp system, it actually departs from it in several important respects.

The new food stamp system is based on the concept of using the national average error rate as the standard and subjecting to potential sanction liabilities those states whose error rates exceed the average. In addition, the food stamp system takes note of the fact that the official state error rate figures released by the federal government each year are *not* precise measures of each state's error rate, but simply represent estimates of these rates. The state error rate figures are only estimates of the actual state error rates because of the inherent uncertainties involved in sampling a small number of cases and projecting the error rate found for this sample of cases to a state's entire caseload.

The state's true error rate may be lower or higher than the "official" error rate figure derived from this sampling procedure. There is what is called a "confidence interval" -- or a margin of error -- around each "official" state error rate figure. For example, if a state's error rate is said to be 8 percent, it may mean that we can be 95 percent confident the state's true error rate lies somewhere between seven and nine percent. In this sense, the state error rate figures derived from the quality control sampling procedures are like the results from political or public opinion polling -- they are estimates which themselves are subject to error, especially if (as is often the case with AFDC quality control procedures) the sample sizes are small.

Many analysts and statisticians have long expressed reservations about the potential inequity of sanctioning a state based on its "official" error rate, when its true error rate may be lower. As a result, proposals have been made to use (for purposes of determining sanction liabilities) the error rate percentage at the lower end of the "confidence interval" surrounding each state's official error rate. Last year's Evans bill, this year's Moynihan bill, and the just-introduced Matsui bill all adopt this approach.

The food stamp legislation enacted last year adopts a somewhat different approach. It continues to use the "official" state error rate figures (rather than the lower end of the confidence interval) but sets the sanctioning threshold at the national average error rate *plus one percentage point*. The confidence interval around the official state error rate figures is often about two percentage points wide. Hence, setting the threshold at the national average error rate plus one percentage point assures that few states whose true error rate is actually below the national average will actually be

sanctioned. It accomplishes this goal while avoiding various technical and administrative difficulties that are associated with use of the lower end of the confidence interval for purposes of determining state sanction liabilities.

This approach has another virtue as well. Tying the threshold to the national average error rate should ensure that the threshold moves down over time as the national average error rate decreases.

I would recommend that the Subcommittee consider setting the sanction threshold for any fiscal year at the lowest national average error rate that has been announced by HHS as of the start of the fiscal year, plus one percentage point. Under such an approach, the threshold would come down whenever the national average error rate decreases, but *not* go back up if the national average error rate should rise. This approach would also enable states to know at the beginning of each fiscal year the error rate level which they must achieve to avoid a potential sanction liability for that year.[1]

Underpayments

Another feature of the food stamp system which I would urge the Subcommittee to consider adopting is the inclusion of underpayments in the basic sanction mechanism. Our message to state and local welfare agencies should be a clear one: the goal is accuracy, and families should receive neither more *nor less* than the amounts to which they are properly entitled. The current system fails to achieve this balance. It effectively says to states: "when in doubt, reduce or deny benefits."

Under the new sanction system enacted for the food stamp program, each state's overpayment and underpayment rates are *added together* -- and the total is then measured against the sum of the national average overpayment and underpayment rates, plus one percentage point. Such an approach treats overpayments and underpayments equally and is simple to administer.

Several of the pending AFDC reform proposals make progress on integrating underpayments into the QC sanction system -- but ultimately all of the pending proposals fall short. The Reagan Administration proposal essentially ignores underpayments. The Moynihan and Matsui bills set up a separate set of measurements and sanctions for underpayments, but do so in ways I believe to be largely unworkable.

Under the Moynihan and Matsui bills, the thresholds (above which underpayment rates can subject a state to sanctions) are set sufficiently high that a number of states with above-average underpayment error rates would probably not be subject to sanctions; this is a considerably more lenient standard than that which would be applied to overpayments. Moreover, the "penalty" for an excessive underpayment rate would simply be that the "sanction amount" would somehow have to be used for increased benefits or improved administration, a "penalty" that likely would have little meaning. For example, in a year with five percent inflation, a state with an excessive underpayment rate could conceivably raise benefits one percent and claim that this constituted the increased benefit amount required because of its underpayment rate. In all likelihood, states would simply claim that modest benefit adjustments they were going to make, anyway, constituted their compliance with this provision.

I believe the only way to handle underpayments that is both workable and balanced is to treat underpayments and overpayments identically in all respects -- by combining a state's overpayment and underpayment rate into one combined payment accuracy rate, as the new food stamp system does. In this way it can be assured that a

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[1] Under the food stamp sanction system, the sanctioning threshold for a given fiscal year is the lowest national average error rate achieved for any fiscal year (including the year just starting), plus one percentage point, rather than the lowest national average rate that has been issued as of the start of the new fiscal year. This is unfortunate because it prevents states from knowing their error rate target for the coming year. Sounder management is promoted when goals and objectives are clear from the outset.

sanction system will be evenhanded with regard to both overissuances and underissuances.

I would note that at present, data are not available to allow inclusion in the underpayment error rate of those underpayments that result from the improper denial or termination of benefits to eligible families. There is evidence that wrongful denials and terminations represent a serious problem and may be more widespread in AFDC than they were a number of years ago. The Matsui and Moynihan bills require a study of how best to collect data on wrongful denials and terminations and also require the eventual incorporation of these data into the error rate and sanction standards. I strongly urge adoption of such a provision.

Error Rate Measurement Issues: Technical Errors

I would also urge the Subcommittee to reform the current rules in AFDC regarding technical (or procedural) errors. The current AFDC rules in this area conflict with those in other programs such as food stamps and Medicaid and have no sound analytic base. The National Academy of Sciences panel, as well as most independent analysts, believe the current AFDC rules to be flawed and inequitable.

Technical errors are those errors that, if corrected, would generally have no effect on the amount of benefits paid. They thus differ sharply from errors that, if corrected, would have resulted in a different benefit level.

Failure to report income, for example, is a *non*-technical error. Had the income been reported, the family's benefit level would have been reduced. The story is different when a technical error occurs. For example, if a QC review finds that a monthly report form is missing from a casefile but the family's income and assets levels are properly recorded in the file -- and that the family's benefits are thus at the proper level -- correction of the error would have no impact on benefit payments. Had the monthly report form been in the casefile, the family would have received precisely the same amount of benefits.

In the food stamp program, a technical error -- such as the lack of a signature on an application form or the lack of a work registration card, Social Security number, or monthly report form in a casefile -- is not itself counted toward the overpayment or underpayment error rates. However, if the QC reviewer finds that the recipient actually has unreported income or an unreported family member (the type of problems that monthly reporting and use of Social Security numbers are designed to avoid), this does count toward the state's error rate. (Similarly, if a household has refused to comply with a work requirement and was supposed to be disqualified, but the state failed to institute the sanction, this, too, would count as an error.) The critical question is whether correction of the error would have affected the amount of the benefit.

It should be emphasized that the food stamp program does *not* ignore these technical errors. They are recorded in quality control reviews as "deficiencies" and reported to USDA. If a pattern of deficiency shows up in a state, USDA requires corrective action. If sufficient corrective action is not taken, the Secretary is empowered to suspend or cancel an appropriate portion of the federal share of the state's administrative funds. This authority can and has been invoked, as I can attest from experience as a former FNS Administrator. Often, a warning letter threatening the withholding of administrative funds is sufficient to secure corrective action on such a matter.

The AFDC system, by contrast, is rather crude. If a case has a technical error in it, the entire family can be considered ineligible -- and the entire benefit counted as an overpayment -- even though the family actually received the correct benefit level, and its benefits would not have been affected if the technical error had not occurred. For example, if a monthly report form or Social Security numbers were not present in the casefile -- but the data in the casefile on the family's income, assets, family size, and other family circumstances were correct -- the entire benefit paid to the family would still be considered erroneous under AFDC quality control procedures. Worse still, in

many areas, the family would be required to pay its entire benefit back, on the grounds that the benefit represented an erroneous overpayment.

In my view, the AFDC policy of counting technical errors as overpayments, and considering the entire benefit provided to the individual (or in some cases, the family) as an erroneous payment, is not justifiable. If sanctions are to be applied for erroneous payments on the grounds that federal dollars have been misspent and must be recovered, then it is inappropriate to make states pay back amounts that have not in fact been misspent -- and that would have been paid out, anyway, if no technical error had occurred.

The principal argument advanced for including technical errors in the payment error rate is that state failure to comply with federal eligibility requirements must be dealt with -- or else these requirements cannot be enforced. This argument is very weak. No one disagrees that federal requirements in such areas as collection of social security numbers and WIN registration must be enforced -- and states penalized if they perform inadequately. But lumping such deficiencies into overpayment rates and levying QC sanctions based, in part, on such deficiencies are wholly inappropriate mechanisms to deal with this issue. Payment error rates should reflect true overpayments, not administrative deficiencies that generally do not carry a dollar impact. There are other methods available to the federal government to deal with administrative deficiencies committed by states, as the approach used by the food stamp program clearly demonstrates.

The NAS Review of this Issue

In testimony before the National Academy of Sciences panel in 1986, the official serving as the HHS assistant secretary at the time made another argument for why technical errors should continue to be counted as overpayments. He contended that these errors are not really "technical" because if work registration cards or Social Security numbers had been obtained, jobs might have been located for participants or unreported income might have been uncovered through cross-checks. This argument, too, is unconvincing. If there is unreported income as a result of a technical error, the income will be uncovered through the QC review -- and an error will be recorded, anyway. This argument thus boils down to a contention that in cases where a Social Security number (or monthly report form) is missing but there is *no* unreported income to be found, an overpayment should still be charged against the state.

This argument is equally thin when it is applied to cases in which a work registration form is missing from the casefile. In some such cases, registration has in fact taken place -- and the problem is one of a misplaced or misfiled document. Moreover, even where registration has not occurred, the likelihood that a recipient might have been placed in a job if only registration had occurred is rather small. Data from the evaluations conducted by the Manpower Demonstration Research Corporation show that state welfare-to-work programs increase employment rates among AFDC recipients by only three to eight percentage points, hardly a basis for assuming overpayments and substantial losses to the federal government in 100 percent of the cases in which a work registration form is missing.

Indeed, after hearing HHS' presentation, and carefully examining this issue, the NAS panel concluded that the AFDC position was unsupportable and that the food stamp approach should be followed. The panel noted:

> "Procedural requirements generally provide some form of internal control, much like the separation of duties or the reconciliation of bank statements with ledgers in financial operations. Such internal controls may reduce the risk of financial loss, but *the failure to follow such requirements does not, by itself, represent an actual loss* -- nor does the adherence to those requirements ensure the avoidance of an erroneous financial transaction (emphasis added).

> ". . . . A good example of the misuse of technical errors comes from AFDC. WIN registration of certain AFDC recipients is a requirement of eligibility, but the fact of WIN registration alone does not ensure that appropriate or effective training or work experience is received. Indeed, the program objective -- relevant and effective training -- may be subverted, through (for instance) the automatic registration of all covered recipients, when WIN registration does not ensure WIN participation. The panel is aware of at least one state that has taken this route, in order to avoid AFDC QC-based "payment errors," regardless of the effectiveness of such registration for recipients."

Even more striking, in a major study of the food stamp quality control system issued in 1987, USDA came to the same conclusion as the NAS panel rather than to the rather tortured position advanced by HHS. USDA noted that procedural deficiencies, such as a missing signature on an application, lack of a work registration card, or lack of information on Social Security numbers

> ". . . do not necessarily lead to an incorrect benefit. Such errors could indirectly contribute to issuance errors, since they might be indicative of systematic problems in administering the program. If this is the case, *the QC system will capture these errors where they matter -- that is, when benefits are incorrect. Correcting the procedural error itself would not alter the eligibility or benefits of the household. Excluding purely procedural errors from the error rate is consistent with the intent of the food stamp QC system to measure the rate of erroneous issuance*" (emphasis added).

New research on technical errors and AFDC error rates

I dwell on this issue of technical errors for one other reason as well. Last year, HHS published a study of the AFDC quality control system in which it reported that AFDC error rates had risen significantly in FY 1986. The report blamed the Congressionally enacted moratorium on AFDC sanction collections for this increase in error rates.

The report, prepared under the direction of a panel of political appointees from several federal agencies and departments (a highly unusual arrangement for an analytic study of this nature), provided no supporting evidence for this contention. Our staff at the Center on Budget and Policy Priorities has conducted research on this issue and has been unable to find any evidence to corroborate the HHS claim. What our research has turned up instead is a finding that a change by HHS in the types of technical errors counted as overpayments -- under which certain technical errors began being counted as "overpayments" for the first time in FY 1986 -- appears to have had more to do with the increase in AFDC error rates than the moratorium did.

The moratorium was enacted in April 1986, when FY 1986 was already half over. Moreover, a moratorium on the collection of food stamp sanctions was also in effect during this period and the food stamp error rate declined, reaching a new low. Why would a moratorium lead states to relax administration of the AFDC program -- a program in which they pay part of the benefit costs and share in benefit losses -- but not to relax administration of the food stamp program, in which the benefits (and the losses) are 100 percent federally funded? The HHS report fails to answer or acknowledge the existence of this issue.

While the HHS report attributes responsibility for the increase in error rates to the existence of the moratorium, and does so without supporting analysis or evidence, the report neglects one of the more likely contributing factors to the error rate increase. Beginning in FY 1986, technical errors related to monthly reporting were counted in state AFDC overpayment rates for the first time.

We contacted six of the states whose error rates climbed most steeply between FY 1985 and FY 1986. Three of these six states reported that their analyses of their error rate increases had found inclusion of monthly reporting technical errors to have

been a significant contributing factor.

For example, Texas' payment error rate climbed from 4.29 percent to 7.47 percent during this period. According to the information we received from the state, monthly reporting errors accounted for nearly one-third of the increase. Ohio could not estimate the precise effect of monthly reporting technical errors on its error rate, which rose from 6.63 percent in fiscal year 1985 to 9.44 percent in fiscal year 1986. But the state reported that monthly reporting, while not the sole cause of the increase, was the strongest single influence on the rise in its error rate. In Maryland, the AFDC error rate rose by about two percentage points between fiscal years 1985 and 1986, from 7.08 percent to 9.20 percent. According to the information provided by the state, errors associated with monthly reporting comprised a little more than one percentage point of the state's 1986 error rate and thus accounted for about half of the error rate increase from the previous year.

Double-Counting of Errors

Inclusion of technical errors in the AFDC overpayment rate is one of several ways in which the current sanction system requires states either to pay the federal government back for losses that did not actually occur or to pay the federal government amounts that are in excess of the loss in question.

For example, this problem also occurs when a state discovers an error, recoups the overpayment from the client, and remits to HHS the federal share of the overpayment. Such cases can show up as errors in the QC error rate, even though the error was subsequently corrected and the overpayment recouped.

This can create inequities among states. Suppose, for example, states A, B, and C encounter three families with identical circumstances. State A certifies the family correctly. State B overissues $100 to the family but subsequently uncovers the error, collects the overissuance, and reimburses the federal government. In neither state A nor state B does the federal government suffer a loss. By contrast, in state C, a $100 error is committed and the overissuance is not recovered. Under the current quality control system, state B will be treated the same as state C -- being charged with an error and sanctioned for a loss of federal funds. Yet no loss of federal funds actually occurred in state B. State B should no more be made to pay the federal government back for its "loss" than should state A.

The Matsui and Moynihan bills would resolve this inequity by specifying that a state's sanction liability would be reduced by the amount of the overpayments the state has remitted to HHS.

A final area in which losses to the federal government are overstated -- and sanction amounts are inflated -- involves cases receiving both AFDC and food stamps. Suppose a household has $100 in unreported unearned income which is discovered during a QC review. The QC reviewer records a $100 AFDC overpayment, as he or she should. However, the reviewer then proceeds to measure the accuracy of the food stamp payment by counting as income both the $100 in unearned income that was not reported and the AFDC benefit amount that was actually paid. This results in the QC reviewer finding an additional $30 overpayment in food stamps. Yet if the $100 in unearned income had been properly reported and counted, the AFDC payment would have been $100 lower -- and the food stamp benefit level would have been unchanged. Counting both the unreported income and the uncorrected AFDC benefit payment thus results in the state being charged with a total overpayment of $130 when the true overpayment (and the loss to the federal and state governments) actually amounted to $100. Furthermore, the determination of QC sanctions is then based on the $130 figure, and $130 is the amount the recipient is asked to pay back even though the overpayments made to the recipient totalled $100.

The National Academy of Sciences panel noted this inequity and called for its correction. The panel observed that the current procedure "results in an overstatement of the loss to the federal government."

Adjustments in error rates to reflect variations in state caseloads

Under current QC sanction systems, all states are required to meet the same error rate standard, without any adjustment for state-to-state caseload differences that are beyond a state's control. The NAS panel recommended that adjustments be made to reflect those key demographic or economic variations in state caseloads that significantly affect state error rates. I support this recommendation.

The NAS panel reported that "data show differences [among states] in error rates on several dimensions, particularly those related to cases with earnings. . . AFDC and Food Stamp households with working recipients, for instance, are known to be much more error prone than other households." An HHS study of AFDC errors, published in 1986, found the AFDC error rate to be nearly three times higher among families with earnings than among those without earnings. A state in which families with earnings constitute a larger proportion of the AFDC caseload would be expected to have a higher error rate than a state with a smaller proportion of working AFDC families.

Consequently, some adjustment in the sanction mechanism to reflect major variations among states in a few key caseload characteristics found to bear on error rates -- such as the proportion of a state's caseload consisting of families with earnings -- appears to be warranted. As the NAS panel observed, "a state welfare agency has no control over the demographic characteristics or economic circumstances of the state itself."

It should be noted that another key characteristic that the data in the HHS study suggest is associated with higher error rates is the degree of urbanization. A typical urban area was expected to have an error rate 3.1 percentage points above the predicted national average error rate.

The Overall Goal

Finally, in designing a reformed error rate sanction system, consideration needs to be given as to the system's fundamental goal: is the goal to be management improvement and long-term error avoidance, or is it the collection of large sums from states so that these funds may be deposited in the federal Treasury? If the principal goal is management improvement, as I believe it should be, this has some consequences for the design and administration of a sanction system. Let me illustrate this point with an example.

In the late 1970s, while I was at USDA, we targeted the five states in which we were losing the most money through excessive food stamp errors. In each state, we withheld or threatened to withhold significant amounts from the federal share of the state's administrative funds. We informed the state that it could avoid the withholding of some or all of these funds -- or earn funds back if they already were being withheld -- upon satisfactory completion of a rigorous set of actions designed to make a major impact on its error rate.

The initiative bore results. In these five states, major error reduction actions were taken that generally dwarfed most state actions that had been taken in the past. As a consequence, food stamp error rates declined significantly, saving the federal government tens of millions of dollars in future years. By taking these actions, nearly all of these states either avoided the imposition of sanctions or earned back the funds we had originally withheld. My point is that our primary goal was not the collection of large amounts of money for past errors, but rather securing decisive improvements in program management so that high error rates would not recur in the future.

In recent years, the federal government has largely abandoned approaches such as this. Instead, the federal bureaucracy has, in my view, relied too heavily on automatic QC sanctions and has done relatively little to utilize the *threat* of sanctions in creative ways to secure management improvements. I would urge the Subcommittee not to build

too much "automaticity" into the imposition and collection of QC sanctions, but rather to allow room for federal managers (and state managers, as well) to use the threat of a sanction to secure large-scale management improvements that might not otherwise be possible. We found that the threat of a sanction sometimes enabled a state welfare commissioner to secure resources he or she could not otherwise get to install a new computer system, secure more staff to investigate possible error or fraud, follow up on "raw hits" generated by "wage matches," or take other needed steps to drive down overpayments. By contrast, if the sanction is "automatic," then not only may the federal government's leverage over the state be reduced, but the total resources available to the welfare commissioner to make improvements may also be diminished, rendering corrective action more difficult. This is not to argue that sanctions should not be collected; to the contrary, there may be many circumstances in which collection of a sanction is necessary and important. My plea here is simply to ask the Subcommittee to build some flexibility into this process so that we do not lose sight of the larger goal of management improvement.

Acting Chairman DOWNEY. Mr. Miller.

STATEMENT OF CHARLES A. MILLER, COVINGTON & BURLING, WASHINGTON, DC

Mr. MILLER. Thank you, Mr. Chairman.

I appreciate the opportunity to speak to the committee this afternoon and I ask that the written statement that I have submitted be included in the record.

Mr. Chairman, I have been an attorney representing States in the area of quality control sanctions for some 17 years.

During that time, I have had an opportunity to see this program go from its inception to the crisis point that it has reached today.

In that period of time, I have had the opportunity to form some conclusions about the basic deficiencies of the system and how it might be corrected to make it achieve its purpose, which is to improve program management and not the imposition of fines on States.

Whatever else may be said about the system and the dubious value of the results that the statistical samples reveal, I think there is even a more fundamental flaw in the present system; that is, the sanction system inquiry ends now where it should begin.

Let me try to describe what I have in mind there and explain to you how I think this problem can be resolved.

The quality control system, when it was first adopted and since that time has been defended as a model of what industry does, mirrored on quality control processes that were developed in industry, particularly in the manufacturing industry to detect errors and to improve and eliminate deficiencies in manufacturing processes. The theory is that we would use statistical sampling as it is used in industry where sampling was a known and commonly used method for identifying problems and in that respect is where I think the flaw lies because in industry the results of statistical samples are used to identify problems.

They are the beginning of an analysis to decide whether corrective steps should be taken.

But in the QC process, inquiry ends with the completion of the sampling and the derivation of an error rate, whereas in industry, the error rate indicates to you whether you have a problem and if so, you then set about analyzing the problem, dealing with it looking at all the factors and deciding if the problem is serious enough to warrant corrective action.

Here, in this program, that threshold step becomes the final answer, and the preliminary number that the sampling process reveals is then exalted into the final answer and gets projected into a universe which produces a tremendous dollar sanction and that is attempted to be imposed upon States as the solution to the inquiry. It should have been just the beginning.

After all, an error rate, particularly a sample based one, may tell you lots of things about State program performance if you look at it in some kind of context.

Over a period of time, a single error point if put on a chart, would reveal a constantly declining error performance which would indicate strong efforts by the State to improve its program.

It could be a blip on an otherwise steady start indicating perhaps aberrational factors or extraordinary external circumstances that impacted the performance of the State that year, or it could be part of an upward trend showing a performance was less than it ought to be.

The error rate established by the system doesn't give you the answer. It only tells you whether you have a problem, and it should be the beginning of analysis, not the end of analysis.

A big flaw in the present system is that there is never a judgment made, no opportunity to analyze all the circumstances and have a decision made by a responsible individual or body as to whether a State's performance has, in fact, been below standard and so below standard as to warrant some kind of penalty or sanction.

That is what the system is designed to yield for us after all.

I have stated the problem. Is there a solution to it? I think there is.

I think the solution can be found in part in the legislation that has been offered by Senator Moynihan and Congressman Matsui.

I take as my starting point the standards set forth in Congressman Matsui's bill setting forth a program for dealing with backlog cases. That is a process for determining whether there has been a pattern in the State of real avoidable misspending of Federal dollars.

After all, a sanction ought to be directed at that, not some mystical calculation of a sample number which may or may not relate to accuracy.

Mr. Matsui's bill establishes for the backlog cases a process that goes about as follows: A threshold is established, and we have all agreed that a threshold needs to be properly established.

Under Mr. Matsui's approach, once the threshold is established, those States whose error rates are above that threshold are then required to go into a further process involving one of thorough analysis and consideration of all the relevant factors to determine whether there, in fact, is a cause for a penalty or sanction.

That bill, I think, wisely identifies an objective, independent and competent agency, to make that determination.

In this case, it is the Departmental Appeals Board, which, though an arm of the Department of Health and Human Services, has over the years established itself as a body of high competence and independence from any constituent agencies in resolving disallowance cases.

Over the years, that body has earned a very high degree of respect and it is the model often pointed to for an example of how Government agencies ought to work.

That board would look at all the factors, and let me touch on a couple of things that we think would be pertinent for that board to consider in deciding whether or not a sanction should be imposed.

It would look at the result over time. That is what the term pattern refers to, so that you are not basing a very important judgment on one single item of information, but rather that information in the context of a State's performance over time so that you could determine whether the results in a particular period were aberrational or reflective.

There would be examination of whether there was actually an error rate of the kind that has been assessed.

We look at the statistics that produced an error rate for that State in the period and make sure there is nothing about that calculation that is unrealistic.

Next, the proposal looks at whether the errors that were found were avoidable.

We know, for example, that in the QC system errors are assigned when the caseworker does the job exactly as he or she is supposed to do, but later, information becomes available that indicates that the payment is more or less than it should have been.

For example, the computer matches often do not have information that is current when the eligibility worker has to make the decision, but the QC worker later discovers information in the computer file that indicates that a mistake was made.

That was not an avoidable error and that ought to be looked at.

We ought to look to make sure the cure for a pattern of errors isn't more costly than the problem itself, so that you can correct a dollar error only by a $10 expenditure. That would not be a wise use of funds.

We look to see whether there is actual misspending. Has there been real mistaken expenditure of Federal dollars, the technical error point has been almost beaten to death here, but that is an example of an error that does not involve misspending and should not involve a sanction.

Sanctions should be as a result of QC reviews. The test ought to be whether the worker followed the instructions given to him or her at the time.

There should not be double penalties. If a misspending of AFDC dollars results in a lower food stamp benefit, that should be taken care of so that States don't get penalized twice for a single mistake.

All that goes under the heading of what is actually misspending. This process would also look at corrective action efforts that a State had taken to determine whether the State's administrative efforts over the years had been what is expected or whether they have been lax.

Mr. Chairman, I think that that sort of approach to solving the backlog problem is far more rational, far more intelligent, and far more consistent with the objectives of the program, which is to promote good administration, than the present system, which does produce sanctions that have no relation to actual misadministration and, in fact, we know no relation to the misspent dollars in the program.

It would be a substantial step forward and I urge that the committee give it its consideration.

Acting Chairman DOWNEY. Thank you.

[The statement follows:]

STATEMENT OF CHARLES A. MILLER, COVINGTON & BURLING

Chairman Downey, Members of the Subcommittee, Ladies and Gentlemen.

Thank you for this opportunity to testify today on reform of the Aid to Families with Dependent Children quality control system.

My colleagues and I have represented state governments on quality control issues in the AFDC, Medicaid and Food Stamp programs since 1972 in an effort to protect states from unwarranted penalties assessed by inequitable systems. I am pleased that you have convened this hearing today and that there appears to be a prospect of real reform of the AFDC QC system this year.

I. INTRODUCTION

Forty-nine states, together with the District of Columbia and Puerto Rico, currently face undeserved penalties collectively amounting to $1.2 billion in the AFDC program. These penalties keep skyrocketing each year, surging to an estimated $2.5 billion through FY 1989. The penalties are the product of the so-called "Quality Control" ("QC") system which purports to determine the rate of state misspending in the Aid to Families with Dependent Children ("AFDC") program and levies penalties based on that determination. This system has been condemned for its gross inaccuracy by the National Academy of Sciences, the National Governors' Association, the American Public Welfare Association, the National Association of State Budget Officers, and advocacy groups representing the low-income populations the welfare program is intended to serve. Because of the grave concerns of its members about the system, Congress has three times imposed a moratorium on the collection of the sanctions.

The present QC system must be replaced, for its does not accomplish its intended purpose of identifying instances of poor program administration warranting a fiscal sanction. Instead, the system produces enormous penalties on almost all states each year that disrupt efficient fiscal planning, demand inordinate time spent on dealing with the sanction issue, and, if they were ever actually collected, would cripple states' ability to provide vital aid to the needy.

The states believe that a sound, rational and fair sanction system is possible. Such a system would use the sample-based error rate as similar calculations are used in industrial quality control processes that supposedly inspired the present system--to indicate cases of possible problems that warrant further consideration and analysis. The major flaw in the present system is that it takes the result of what should be a preliminary step--the calculation of an error rate based on a sample of cases--and exalts it into the sole determinant of the ultimate penalty. The Department of Health and Human Services perpetuates the flaw by refusing to use the waiver process to ameliorate the worst characteristics of the present system.

A sound QC system would be based on criteria for evaluating state program administration that were set forth in the law, and a qualified, objective and independent body would apply those criteria in evaluating those cases where the sample-based error rate exceeded a statutory threshold and thus indicated a need for further consideration. The Moynihan bill (S. 231) and the Matsui bill (H.R. 2243), taken together, supply the framework for such a system. The states support

efforts to use these two bills to establish such a system, which would finally end the interminable debate over the failings of the present QC system.

II. BACKGROUND

When the QC system was first developed in the 1960's, the states welcomed it. The system was intended as a management tool to identify problems in welfare administration and facilitate corrective action. The cost of the AFDC program is shared by the states and the federal government, and both sides recognized their common interest in avoiding errors in payments to welfare recipients. In the ensuing years, however, the QC system's original purpose of providing management information has been largely lost in the effort to use the system for the imposition of program-wide penalties on states. Recently, in the face of a mounting federal deficit, there have been concerns that QC was being used as a back-door means to reduce federal support of the AFDC program, notwithstanding the calamitous impact such a policy would have on the nation's poor.

The QC system purports to measure states' accuracy in paying welfare benefits. As one of the most complex public endeavors, the AFDC program cannot be administered error-free. Eligibility workers struggle under tight time constraints to investigate the scores of factors that determine eligibility and benefit amounts. It is in this context that the QC system attempts to identify the "errors" made by states in determining eligibility and benefits and to calculate a payment error rate.

However, clearly there is something fundamentally wrong with a system that finds that only one state consistently complies with program requirements. As summed up by Senator Evans in testimony before the Senate Finance Committee in October 1987: "Anytime you have a program where 49 out of the 50 States are under sanction . . . that indicates . . . that the system itself is giving us the wrong answers."

III. THE NECESSITY FOR REFORM OF THE QC SYSTEM

The states, no less than the federal government, are committed to ensuring accountability in the administration of the AFDC program. The states share the cost of the program, and they are as keen as the federal government to guard against misspending. The sharp decline of payment error rates since the 1970's (with the greatest reduction achieved before adoption of the present QC system in 1981) testifies to the states' determination to reduce erroneous payments and their commitment to invest considerable resources to achieve that goal. The states support quality control, but they seek to be evaluated by a system that yields a reasonable and reliable measure of their performance.

The current QC system fails to meet this standard. It is riddled with biases and inaccuracies, and the error rates it generates are essentially worthless as indicators of state performance. The fundamental problem of the current system is that it takes what ought to be step one in a rational quality control system and stops there. Even industrial quality control processes upon which the AFDC QC system was supposedly modeled begin inquiry into a problem when a statistical analysis suggests an error has been made. Industry takes further steps to analyze the circumstances

surrounding the so-called "error" to determine the true quality of performance. The importance of evaluation and judgment based on a full factual review, rather than slavish reliance solely on the results of sample-based statistical reviews, has been emphasized in the writings of the leading scholars in the field of quality control processes.*/

In AFDC, we have a system that measures a state's administrative performance using a highly suspect methodology, and then assesses sanctions on an automatic, anonymous, formula-driven basis. Judgments are never made by real people to determine whether there has, in fact, been a pattern of actual, avoidable misspending of federal dollars.

Furthermore, the present system employs blinders in using the data that it does produce. A single error rate is calculated for a one year period, based on state reviews, federal re-reviews (that do not always use the same standards that governed the eligibility decisions of state workers), and a highly suspect regression formula. That single rate is the sole basis for the penalty calculation. No heed is given to rates for prior or subsequent periods, or to the trend of error rates within the one-year period.

That single error rate, if looked at more broadly in the context of other available information, could have widely different meanings. For example, if considered together with error rates for several years, it could show that the state's performance has been improving steadily over time; it could show that the rate for the one period in question was aberrational indicating extraordinary circumstances applicable to that period, and revealing that the state's pattern of error rates is actually much different; or it could demonstrate that the state's performance is steadily worsening, in which case a sanction may be warranted. Without further analysis, the single error rate, even if it were an accurate reflection of performance during the particular period does not permit a conclusion about the quality of a state's performance with regard to the spending of federal funds, and most certainly does not tell us how much a state should be sanctioned.

Under an intelligent and rational quality control system, once the statistical methodology suggests a problem, a further examination must be conducted on a case-by-case basis by individuals who can be held accountable for their decisions to sanction states.

IV. LEGISLATIVE REFORM PROPOSAL

The backlog of sanctions covers fiscal years 1981 through 1986, which is as far as DHHS has gone in calculating payment error rates. S. 231, the AFDC Quality Control Improvement Act of 1989, introduced by Senator Moynihan, proposes to resolve the backlog issue by sanctioning states whose error rates (after certain adjustments are made) fall outside a threshold to be established by Congress in

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*/ See Deming, W.E., Quality, Productivity, and Competitive Position (MIT 1982), pp. 111-118; Juran, J.M., Managerial Breakthrough (McGraw Hill 1964), pp. 301-308; Juran, J.M. and Gryna, F., Jr., Quality Planning and Analysis (McGraw Hill, 2d ed. 1980), pp. 3, 35.

consultation with HHS. That threshold may be the national average or some different figure.

This proposal places unnecessary burdens on the Congressional committees in resolving past disputes. Furthermore, it only helps to identify the most obvious cases of improper sanctions and fails to adequately ensure that a state will be sanctioned for past years only if a sanction is actually warranted. An additional process is needed to examine the situation of the states above the Moynihan threshold to determine whether these states should be sanctioned and for what amounts.

Congressman Matsui's bill, H.R. 2243, contains a proposal for resolving the backlog of sanctions that incorporates the principles articulated above, that the quality control system should determine whether a state has a pattern of actual, avoidable misspending of federal dollars. The proposal authorizes the Departmental Appeals Board -- an objective, competent and widely respected body of officials within DHHS with experience in the quality control area -- to examine the case of each state that would fall above a threshold set by Congress. Rather than a faceless, bureaucratic formula spewing out sanctions of such magnitude that none have been collected in nine years, the Board would assess a state's performance under criteria set in statute yielding a decision on a sanction amount that would likely be more reasonable and defensible.

The Board's inquiry would follow the standard used by the National Academy of Sciences: performers should be held accountable only to rules that were known in advance and for procedures over which they have control. The relevant factors to be considered by the Board would include:

> (i) whether the determination of the State's error rate is sufficiently reliable, from a statistical point of view, for a conclusion that the State's error rate exceeds 0.06, or whether such determination yields a higher error rate than would result from an unbiased statistical methodology;
>
> (ii) whether the errors for which the State is cited represented net misspending of benefit funds;
>
> (iii) whether the error rate was affected by factors beyond the State's control, such as caseload growth, caseload composition, program changes, strikes, or natural disasters; and
>
> (iv) whether the State's record with respect to corrective action demonstrates a reasonable concerted effort to reduce errors.

This Departmental Appeals Board proposal should supersede appeal to the Secretary under the waiver process, which has proven totally ineffective. The states have expended enormous staff time to compile elaborate waiver requests under the guidelines set forth in regulations. Again, because DHHS has resorted to an anonymous, form-driven system, the response to the waiver requests has been totally without a reasonable basis. Of the waiver requests that HHS has thus far decided (for years 1981-1984), HHS has waived only 10 of the 141 sanctions imposed. In fiscal years 1982 and 1983, no waiver requests were granted at all. The states believe that in order to yield a more

rational result, the Board must be authorized to hear these issues.

Appealing cases directly to the Departmental Appeals Board would significantly shorten the time it takes to complete the administrative decision-making process. Under the Matsui proposal, the statute would spell out the criteria the Departmental Appeals Board should follow. Such statutory guidelines should help expedite the review process. Moreover, the Board has demonstrated its ability to handle complex funding cases under the public assistance programs in a timely and efficient manner. Under these circumstances, it is reasonable to assume that a decision could be rendered by the Board as early as six months after a hearing is held.

Under the present system, however, there are over 120 cases pending before the Secretary. All will go to the Departmental Appeals Board for further review once the department finalizes the disallowance process. While the Board's scope of review appears to be quite limited, a state has to go to the Board first in order to exhaust its administrative remedies. Under these circumstances, the Board will have to process over a hundred cases before the court can deal with the major issues presented by these cases.

Based on past experience, it will likely be at least two years before the Board can process all these cases; judicial review is virtually certain if the Board does not set aside the sanctions.

If the Matsui approach were followed, this clogging of the administrative process and undue delay of final determinations of sanctions would be eliminated. There would be far fewer cases before the Board, and the Board would have full authority to review all relevant issues. Judicial review, as in other categories of cases handled by the Board, would likely be the exception rather than the rule.

Thus, we think the Matsui approach is far preferable to current law, and forms a sound basis for restructuring the AFDC quality control system.

Acting Chairman DOWNEY. Ms. Smith.

STATEMENT OF ALICIA C. SMITH, DIRECTOR, COMMITTEE ON HUMAN RESOURCES, NATIONAL GOVERNORS' ASSOCIATION

Ms. SMITH. Thank you, Mr. Chairman.

It is a pleasure to be here this afternoon. I would like to carry with me the personal regrets of Governor Campbell that he couldn't be here today. There was an unavoidable conflict in the State that kept him at home.

I would like to also ask that my written statement be submitted for the record.

I think just a few points that aren't covered need to be mentioned or bear repeating, Mr. Chairman.

First, the quality control system was developed back in the early sixties as a management tool for the States. The purpose of the quality control system was to not only be an audit function for the States, but to assist them in making good management decisions in the efficient and effective use of Federal dollars.

The flaws in the system are obvious. I won't review them except to pick up on a concept raised by Mr. Miller, and that is the relationship between quality controls and improvement system and the way in which quality control is used in industrial and corporate America.

I think many of the Governors these days consider themselves CEO's of large State operations in which they have a product to produce and that product begins with a healthy, well-educated and protected citizenry.

The point that Mr. Miller raised is one of concern to the Governors, that this system stops where a good quality improvement system ought to begin.

It raises a statistical flag and says, based on this flag, we are going to impose severe fiscal penalties on the States rather than giving the Governors and their people the opportunity to ask a series of important questions, what are these errors that are being made, why and can they be fixed in a cost-effective manner and what relationship do they bear to other very important program goals that we are supposed to be accomplishing through the AFDC system?

We have a brandnew program which we were very excited to get from this Congress in the form of a welfare reform program, the JOBS program, that many States are beginning to implement, and there is a great deal of concern that unless we fix the system now and have a management system that is going to be an effective tool for the Governors and their staffs to use as they implement the JOBS program, that the system is only going to get worse.

We are going to compound an already difficult situation in many States. The States won't be able to use the quality control system to gather the information they need to make good decisions about how they run their AFDC JOBS programs.

So I think that is the importance from the Governors' perspective that as the system is reformed, that the statistical signal sends up a flag that gives Governors and their staffs an opportunity to make a series of good human management decisions and that we not be

allowed to hide behind a formula that doesn't take into account a whole series of management decisions and strategies that need to be made.

Starting last year and working in conjunction with the American Public Welfare Association, the Governors put together a policy on the form of the quality control system reiterating first their support for performance accountability in needs test and entitlement programs and not wanting to shirk any responsibility that they have for running these programs in an efficient manner.

I would like to reiterate some of the basic principles from that policy.

First, it is important to understand that both the Federal and State Governments are responsible for administration of the AFDC Program and, therefore, both need to be held accountable for the effective management of the program.

Second, given that the current quality control system serves primarily Federal interests, we believe that a reform system should separate the management and the audit functions of the system.

Third, we believe a State's performance should be assessed according to a Federal-State agreement on program administration that is memorialized in a State plan and if there are problems with that State plan, those problems ought to be dealt with in a compliance proceeding.

We believe that the States' progress in error reduction must be considered.

As Mr. Miller pointed out, you need to look at that statistical dot in time and say what does it suggest about that State's performance over time? Is that a blip on the landscape?

Is that an indication of ongoing problems? Is there something that is along the line of what Greg Coler referred to? Do you have a State with thousands of refugees being dumped on its shores and what kinds of problems does that present?

There are all sorts of issues involved in where that point in time comes for a State.

So it is a system that penalizes States who are the poorest performers or to reward States who are the best performers.

Six, a concept reiterated many times this morning is that States should only be penalized for dollars that are actually misspent.

To penalize States for technical errors which don't result in a difference in the amount of benefits that a family received should not be subject to penalty.

Seven, that States should not be subject to penalties for errors based on information that wasn't available to them at the time that they did the case review.

I think it is important to note that the whole issue of improper denials is of greatest concern to us as the issue of improper payments.

We have roughly 45 days to make eligibility determinations and supply a family with AFDC benefits.

These people don't come to us with cushions, because they are desperate, and because they are one step away from homelessness, from having to disrupt their entire family pattern.

So I think that is an important point.

Eight, that acceptable measures of performance should be based on statistical estimates designated to shift the margin of error in the State's favor and to take a look at the significant program variations and demographic variations within States.

AFDC programs are not alike in all States. They are not even alike in all parts of a State.

It is important to look at the program that is being operated in that State and in a portion of a State and how it is different from the program that is being run in perhaps its neighboring States.

Nine, we believe that States with financial liability should have the opportunity to reinvest in activities designed to reduce erroneous payments; that some portion of the money owed ought to go back to strengthen their management system.

Ten, for its part, we think that the Federal Government should be held accountable for reviewing the reported quality control findings in a consistent and timely manner.

Frequently, the findings of error rate reviews by the Federal Government are not available to the States, sometimes for up to 2 years after the fiscal year has ended and that is not the kind of timely information that enables the States to make the management decisions.

Last, that Federal support is needed to minimize the impact of the Federal program and policy changes on State performance.

I take you up on your offer to try to do an eligibility determination. We will be happy to make that opportunity available.

Very quickly, I would like to echo our support for the proposal laid out by Mr. Miller on how to deal with the backlog issue.

We believe that even though there is a waiver process available to the States now, the States that have applied for a waiver, only six have been granted since 1981 and none in a timely enough manner to enable a single State to get to the Departmental Grants Appeals Board.

We support the notion of statutory authority for the Departmental Grants Appeals Board to review based on a whole series of considerations all of which are laid out in my statement, and I would like to emphasize that from our perspective, this is the year to act.

CBO hasn't scored any money in fiscal year 1990 for quality control sanctions. The moratorium expires in June. We are looking at implementing the JOBS program July 1 and I think it is particularly important for the 19 States that do their budgets according to generally accepted accounting principles where without the congressionally imposed moratorium, thee sanctions would be counted as a liability on the books, and that is a serious financial problem to those 19 States that do their budgets that way.

The Governors are ready and willing to work with you and the committee as you look for the right fix.

Acting Chairman DOWNEY. Thank you.

[The statement follows:]

STATEMENT OF ALICIA C. SMITH
FOR THE NATIONAL GOVERNORS' ASSOCIATION

Good Morning. I am Alicia Smith, director for the Human Resources Group of the National Governors' Association. On behalf of the nation's Governors, I would like to thank the subcommittee for offering us the opportunity to testify this morning about the urgent need for the reform of the AFDC quality control system and to offer our assistance to you to resolve these complex issues in a fair and equitable manner that protects both our most vulnerable citizens and the integrity of federal and state expenditures.

An Historical Perspective

A quality control system for AFDC was introduced in 1964 as a management tool to help states make more efficient use of state and federal funds and to ensure that monies were directed to those most in need of public assistance. The system was revised in 1970 and again in 1981, when the notion of fiscal sanctions for error rates was introduced. Since 1981, the combination of legal action and congressionally enacted moratoriums has prevented the collection of any of these fiscal sanctions. Yet, without the imposition of fiscal sanctions, the states have managed to bring the error rates down from a 1973 high of 16.5 percent to the current low of 6 percent. Yet today, 49 of the nation's Governors are faced with a combination of problems: a seriously flawed system, the expiration of the moratorium on June 30, 1989, and an aggregate of $1.2 billion in outstanding fiscal sanctions.

Flaws in the Current System

Nearly everyone agrees that the quality control system, envisioned in its beginnings as a management tool for states, suffers from serious flaws that not only hinder its ability to be useful for its intended purpose but actually thwarts state efforts to manage their AFDC

programs. Last year's congressionally mandated study of the system by the National Academy of Sciences pointed out many of the major flaws in the system:

- The error rate measurement in the current system is confounded by the inclusion of technical or procedural errors that do not result in overpayments but which nonetheless penalize states through punitive fiscal sanctions.

- The statistical procedures within the quality control system are flawed as a basis for setting fiscal sanctions. Currently the system uses the mid-point of the statistical confidence level to determine error rates, while it is widely recognized that using the lower boundary of the confidence level will eliminate the risk of overestimating state sanction liability and penalizing states for errors they did not commit.

- The current error rate tolerance levels are arbitrary and fail to reflect relevant differences between states and between the different kinds of benefit programs they provide. It is also important to note that the official tolerance level for the AFDC quality control system is lower than for any program run by the federal government.

- The current system ignores valid differences between client-caused error and agency-caused errors, despite the fact that we know that client error accounts for some 45 percent of the average state's error rate. Thus, errors over which the states have little or no control account for almost half of our published error rates.

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Governors As Managers

The Governors today quite properly think of themselves as chief executive officers of their states and approach their jobs in much the same way that a CEO of any major corporation or industry might.

They are concerned with the efficient and cost-effective operation of state government and they are concerned with a product that begins with a healthy, well-educated, and protected citizenry. In that context, Governors, like other CEOs, are concerned that the management tools that measure the performance of their states are useful tools.

In corporate and industrial America, a quality control system that simply measured a statistical sample result and stopped there would be totally unacceptable. The statistical measurement of results would be only the first step in a rational process; it would raise a flag that indicated a problem that needed further examination. Industrial and corporate CEOs would then examine the problem further and ask questions like: Why are these errors occurring? Can they be fixed? Is it cost-effective to fix them? They would apply their best human judgment to the problems raised by the statistical flag and make good management decisions based on the answers.

The AFDC quality control system stops at the first step and responds only to the results of the statistical sample. It fails to go beyond the error rate to determine the reasons for the errors and the cost-effectiveness of addressing those reasons. It obscures the opportunity for good management decisions behind a formula that tries to reduce a very human system to a series of statistical averages. This is a bad business decision.

Given the current nature of the quality control system, it is not a management tool at all but the sword of Damocles hanging over the heads of state managers. If you view the system from the perspective of the Governors as CEOs, a number of problems are obvious:

- The system diverts vital and scarce resources away from clients and from serious management initiatives. The payment of fiscal sanctions will come from those scarce resources.

- The threat of severe sanctions distorts management decisions by forcing states to focus exclusively on payment accuracy to the exclusion of other legitimate and, I would submit, more important program goals. The recent passage of the Family Support Act of 1988 is a case in point. States will be far less willing to take calculated risks in bringing people into their welfare to work programs to achieve the ultimate goal of self-sufficiency if they are hampered by the constant threat of increased error rates and the corresponding fiscal sanctions.

- The current sanction-based system impedes good management decisions because it creates disincentives for states to collect good, accurate management information.

- The system forces the federal government and the states into an unproductive obsession with error rate measurement rather then creating an atmosphere of true partnership to achieve real error reduction.

- Thus, the quality control system fails as a management tool, even apart from its close link to punitive sanctions, because the information that comes through the system doesn't help improve decisions on eligibility, payment amounts, or corrective actions; the federal data is given to the states much too late to be useful as a planning tool; it ignores the cost-effectiveness of rooting out the last error; and it measures so little of what our welfare agencies are actually called upon to do.

Governors' Policy

During our recent winter meeting this February, the Governors unanimously adopted a policy on the reform of the quality control system. That same policy was adopted by the American Public

Welfare Association at its mid-winter quarterly meeting. In our policy, the Governors reiterated their support for performance accountability for needs-tested entitlement programs administered by the states and jointly funded by federal and state appropriations. But the Governors urge you to put in place a fair and equitable system to assess state performance and encourage, rather than inhibit, management improvements.

Toward that end, we would offer some basic principles for the reform of the system:

- Both federal and state government are responsible for administration of the AFDC program; therefore, both must be held accountable for efficient management of these programs.

- Given that the current quality control system processes serve primarily federal interests, a reformed system must separate the management and audit functions.

- States' performance should be assessed according to the federal/state agreement on program administration represented in the state plan. Any discrepancies between state and federal agencies over a state plan or program manual should be dealt with in the compliance process.

- The states' progress in error reduction must be considered. The standards to which states are held accountable should be based on demonstrated state achievement, not arbitrary standards.

- A system that penalizes the states with the poorest performance should also reward those states that perform best.

- States should be penalized only for actual misspent dollars. Technical errors should not be tied to fiscal penalities and state penalties should be reduced by overpayments recovered.

- States should not be penalized for errors based on information that ways not available at the time of the state reviews, but that was available at the time of the federal review.

- Acceptable measures of performance should be based on statistical estimates designed to shift the margin of error in the states favor (i.e. using the lower bound of the confidence interval in lieu of the point estimate in calculating payment accuracy rates). In addition, a fair measure of performance must take into consideration significant demographic and program variations within and across the states.

- States with a financial liability should have the opportunity to reinvest in activities designed to reduce erroneous payments. Similarly, a fair and effective mechanism should be available to provide administrative relief for such states.

- For its part, the federal government should be held accountable for reviewing the reported quality control findings in a consistent and timely manner. More flexibility is needed to enable both the federal government and the states to compensate for inaccurate federal data.

- Federal support is needed to minimize the impact of federal program and policy changes on state performance. Special

attention must be given to simplifying and coordinating the three diverse federal programs. Given program complexity, states should be afforded adequate lead time to implement federal program changes and should not be subject to sanction during the implementation of new policy.

The Backlog

Certainly any effort to reform the current system leads to the question of how to deal with the backlog of sanctions.

Bills currently pending before Congress outline prospective procedures that would identify the most obvious cases in which there is no indication that a state failed to responsibly manage federal funds. However, we believe that additional procedures are needed to assess the remaining states and to determine whether and how much they should be sanctioned. While both current law and the pending legislation allow states to apply for a sanction waiver from the secretary of the Department of Health and Human Services, and to appeal to the Departmental Grants Appeals Board, we do not think this approach is workable.

Of the 49 states currently liable for fiscal sanctions, only six have been granted waivers. Of the states that have had waivers denied, the process has been so slow and cumbersome that not even one has yet been able to appeal to the Departmental Grants Appeals Board.

We would suggest statutory authority for the Departmental Grants Appeals Board to examine, in the first instance, the case of each state that does not qualify for an exclusion from sanctions. The Board would then determine whether sanctions are warranted for that state and the appropriate sanction amount. These determinations would be based on an inquiry of whether, and to what extent, a state's quality control record reflects a pattern of actual, avoidable misspending of federal dollars. Relevant factors to be considered by the Board should include:

- whether the state's error rate is sufficiently statistically reliable for a conclusion that the state exceeded the tolerance level or whether the state's penality is upwardly biased;
- whether the errors for which the state was cited in fact represented misspending of benefit dollars;
- whether the errors for which the state was cited could have been avoided by the state agency by cost-effective means that would not have interfered with program purposes;
- whether the state's error rate is based on errors that are also reflected in the state's error rate for another welfare program or whether the error rate is based on monies that have been previously recouped by the federal government;
- whether the state's error rate history is consistent with the error rate for the period in question; and
- whether the state's record with respect to corrective action demonstrates a concerted effort to reduce errors.

We also urge that states be allowed to seek judicial review of any case where the Board decides that a sanction is warranted. Further, if a sanction is ultimately imposed, a state may fulfill its sanction obligation by investing at least one-half of the sanction amount in corrective actions to reduce errors.

We believe that such a procedure should be implemented to resolve the backlog of cases from 1981 through 1986. If a threshold is set in prospective legislation, that threshold should become the starting point for further determinations by the Departmental Grant Appeals Board.

The Administration's Proposal

The administration has proposed a reform of the quality control system that recognizes a 6 percent tolerance rate for error. While it is encouraging that the proposal sets a tolerance limit at or near the national average, the proposal also calls for prospective payments based on projected error rates. The Governors are extremely troubled by this. To determine and collect monies from states for errors before errors are ever made defies the most basic principles of our jurisprudence system; that is, that one is innocent until proven guilty. We would urge the Congress not to adopt any system that involves prospective payments.

The Time to Act is Now

In closing, I want to reiterate the Governors' sense of urgency that this is the year to reform the quality control system. The fact that the Congressional Budget Office has not scored any sanction collections in 1990, the fact that the sanctions are projected to rise to the level of $2.5 billion by next year, the fact that the moratorium expires on June 30, 1989, and the fact that the states are poised to implement a major new JOBS program in AFDC, all suggest that the time to act is now.

The expiration of the moratorium is of special concern to the 19 states that prepare their budgets according to generally accepted accounting principles (GAAP). This is because GAAP rules could well treat sanction amounts as an accounts payable in the absence of a payment moratorium after July 1, 1989. Our common failure to resolve this issue this year will not only put all states in extreme fiscal difficulty, but leave us with a flawed and unworkable management tool.

As always, the Governors are ready and willing to work with this subcommittee and Congress to resolve this very critical issue fairly and expeditiously.

Thank you.

Acting Chairman DOWNEY. Will you send to all the members of the subcommittee the eligibility forms of their respective States?

Ms. SMITH. I will be happy to.

Acting Chairman DOWNEY. Mr. Coler, I am going to ask you two brief questions.

Florida had its QC rate drop from, I think, 7.9 percent in 1981 to 4.5 percent in 1984, but it is back up to 9 percent in 1986.

Can you give me some idea of why Florida went up?

Mr. COLER. Part of the reason is we doubled the number of people who have earned income. I mentioned that as a result of our implementation of Project Independence, which mirrors the Family Support Act. Those are the cases that have the income attached with them that are the cause of most of the errors.

I believe that, once we implement our famous system for the State, that we will reduce our error rate. That is the only way that I believe we will able to do it given current technical regulations for the program.

Mr. GREENSTEIN. I would add, this is more on the technical error front, in fiscal year 1986, for the first time, HHS required the counting of errors as technical errors connected with monthly reporting.

I know we did not look in Florida, but we looked at six States whose error rates went up the most from 1985 to 1986 and three had done analyses that identified the inclusion of monthly reporting technical errors as one of the principal reasons why the error rate went up in 1986.

So when we say an error rate went up, we need to make sure that true misspending went up, not simply that we began counting non-dollar errors that we didn't count in the past.

Acting Chairman DOWNEY. If the moratorium were to expire and states appealed allowances, how successful do you think HHS would be in collecting disallowances?

Mr. MILLER. Mr. Chairman, even before this time when we had many fewer cases than would now be the norm, it was taking years for the administrative process to be completed. When the moratorium goes off, there will be 120 cases in the pipeline ready for presentation once the final notices are received.

We had 9 cases in the medicaid sanctions and it took the board almost 2 years to decide those—admittedly, the first case of its kind, and I won't extrapolate on a straight line, but 120 cases might take several years for the board to complete the process.

Acting Chairman DOWNEY. Is this a growth industry for Covington & Burling?

Mr. MILLER. It is already a growth industry. The other half of this problem is that the board is limited at the present time in the kinds of issues it can consider, partly at the urging of HHS and partly at the board's analysis, so judicial review of these cases is almost inevitable if they go against the State at the board level.

We feel that if the approach along the line of Congressman Matsui's bill were adopted and the board were given a set of criteria, the board could function and get them all done. Secondly, it wouldn't have 120 cases because you would only have the cases that failed the threshold and you would have less likelihood of judicial review.

Acting Chairman DOWNEY. Mr. Matsui.

Mr. MATSUI. I would like to thank Mr. Miller and Ms. Smith for supporting the concept of trying to look at the backlog from a perspective of a plan rather than on the basis of hard numbers, because I don't think that the States intended to create these problems for themselves; I think it happened because they were getting used to a new system back in the 1970's, and over the late 1980's.

And that is why we have seen a drop in the error rate, but the increase occurred at a time when they were in a very formative stage. So at this time we need a process that will have a plan of action.

Mr. Miller, since you have been involved with this since 1972–73, could you give us a chronology, perhaps an historical perspective on how we got to where we are today, with a $1.2 billion backlog? In fact, the Federal Government hasn't really collected any of the money yet. Perhaps you could comment on that.

Acting Chairman DOWNEY. You have 4 minutes in this sweeping history.

Mr. MILLER. I will use 2 and yield back the rest of my time.

Mr. Matsui, when the original proposal was adopted in 1973, it set tolerance limits and everybody agreed were picked out of the air, 3 and 5 percent. Those were taken to court and the court concluded that they were arbitrarily set and even the Federal Government conceded that.

From 1976, when the court decision was announced, until the end of the 1970's, there was no functioning sanction system in place. It was on the rocks.

In 1980 or so, when, for various reasons, the Michel amendment had impetus, the number of 3 percent was selected and put into a resolution which became law in some people's minds. That is a disputed issue. But there was no analysis, no study, no real rational scientific way for that number to be selected, yet it has been in effect the guideline or the milepost ever since.

It is so unrealistic in the context of the program and what it measures is so unrelated to actual misspending of dollars, that you have created this monster now that churns out, year after year, large numbers of sanctions that aren't measures of real misspending, but they are measures of threatened penalties.

I think we are where we are today because a system has created such an unrealistic situation and such an enormous problem that there was finally recognition that it needs to be dealt with.

Mr. MATSUI. In terms of the Michel amendment, that was offered on the floor, if I am not mistaken. Were there any hearings regarding this issue and the number that the Michel amendment used prior to its being offered on the floor?

Mr. MILLER. No. It wasn't even offered on the floor. It was a double incorporation by reference to something that was dropped into the last paragraph of an appropriations committee report.

Mr. MATSUI. Report language?

Mr. MILLER. Yes.

Acting Chairman DOWNEY. I recall when we came in to vote. The explanation of the vote was that if you wanted to reduce welfare, this was the vote. If you didn't, the vote was no, and that was about the level of analysis that was given at the time.

Mr. Matsui, Are you finished questioning?

Mr. MATSUI. Yes.

Acting Chairman DOWNEY. Mrs. Johnson.

Mrs. JOHNSON. Two quick questions. I thank the panel for their interesting testimony.

Mr. Greenstein, does your formula differ from the one in the Matsui bill? When you talk about adding overpayment and underpayment and comparing that sum to the national average, does it deal with underpayments differently?

Mr. GREENSTEIN. Yes. I have only had the opportunity to look briefly at the bill. I think it is a fine bill. There are a few areas where it could be made better.

My own sense is that the underpayment provisions in the bill would be a paper tiger that doesn't work well for two reasons: There is a separate underpayment threshold in the Matsui bill for underpayments and it is set at a level that is a different kind of standard than for the overpayments. For States that are over the national average minus 1 percent, on overpayments they would be potentially subject to a sanction, but many States under the same circumstance under underpayments would not be.

Second, the remedy wouldn't work. It is that the money be then used for improved benefits or improved administration. I am afraid that in a year with 5 percent inflation, a State could give a 1-percent increase, a 4-percent real drop, say that that 1 percent increase was the overpayment amount, and the issue would then go away.

I think there is no way to make underpayments work right than to treat them exactly the same as overpayments. Whatever you do for overpayments, I would do the same thing for underpayments. I would add them together and measure them against whatever threshold you set.

I think that the minute you have different thresholds and different standards for both and different standards for when you levy the sanction and when you don't, you will make the underpayment part not very real, and it won't be much different than what we have today.

Mrs. JOHNSON. Mr. Miller, to determine who should be sanctioned, would you apply whatever new program we come up with retroactively? Would that be the way you would dispose of the existing back claims?

Mr. MILLER. If you came up with a program that involved a process of rational and careful analysis of the circumstances, and rather than just a mechanical application of a statistical sampling number, then I would strongly support its application to the past, as Congressman Matsui has proposed, and I would think that that kind of solution proposed could also be applied for the future.

It is not that way in the bill now, but it could be and would probably be a more rational way of dealing with penalties in the future than relying upon a statistical system and using the numbers to actually measure the sanctions, because I think that is the core of the problem.

I would use the system to give you the threshold and identify the cases, but I would look at them with an independent body that is accountable and not now as generated.

Mrs. JOHNSON. My point is that if we change the criteria, it seems to me impractical to try to go back and look at the samples on which the error rates were established to see whether or not under the new criteria, those error rates would have been established. So it seems very laborious.

I am looking for something——

Mr. MILLER. You don't necessarily have to go back and redo the samples from the past, as long as you find some appropriate system using the data that is now available to identify the high error cases or at least potentially high error cases.

Once you have identified those cases, then the analysis that would be applied to them by the appeals board, for example, would be a factual analysis on the facts of that particular case. It wouldn't necessarily have to be an analysis of the statistics, but would be an analysis of the performance of a State during that period.

Mrs. JOHNSON. You say that the underpayment information is available in food stamps, Mr. Greenstein. Do you claim that it is also available in AFDC?

It seems to me they are very different programs. Why do you say that the underpayment information is available in AFDC?

Mr. GREENSTEIN. There are two kinds of overpayments and underpayments. Over payments would include payments to people who were really ineligible and paying too much. In underpayments, you pay too little to people who are eligible or you can improperly deny or terminate.

There is no disagreement that no QC system now collects the kind of data that would enable you to determine the dollar amounts not given to people who should have gotten them through improper denials and terminations. There is no question that we would have to have a study of how to incorporate that.

Such a study is in the Hunger Prevention Act for food stamps last year. It is in the Matsui bill this year. I am attempting to distinguish the wrongful denials and terminations from the findings that for active families in the program that got less in benefits than they should have, if it is the case that the AFDC quality control system as it now stands doesn't even collect that information, information we have been able to collect for close to 15 years in food stamps, then someone really hasn't been minding the store.

It also is the case that if in fact AFDC isn't collecting that now, they ought to start doing so immediately and they would not need a study on how to do it. We have done it successfully for years in food stamps. The part that is tricky is only the wrongful denials and terminations.

Mrs. JOHNSON. Thank you.

Acting Chairman DOWNEY. Mr. Shaw.

Mr. SHAW. Thank you.

Mr. Coler, I believe you referred to the system as mean spirited because it does not give States credit for underpayment but merely measures overpayment. Am I correct in quoting you?

Mr. COLER. That would be one reason.

Mr. SHAW. Ms. Smith, based upon your comment that it is equally as important to be sure people get what they deserve as it is to

see that they don't get more than they deserve, would you take issue with Mr. Coler's statement?

Ms. SMITH. I think that would be relatively consistent with what Mr. Coler pointed out, that right now the system is so excessively focused on payment accuracies, that is overpayment, that it doesn't look properly and fairly at the rate of denial to people who are eligible and doesn't bring them into the system, because there is a certain fear of making those kinds of decisions. The tendency is to say no because of the error rate problem as opposed to looking more carefully at whether or not it is appropriate to say yes.

Mr. SHAW. So you think on balance that we should give States credit for underpayment?

Ms. SMITH. I am saying that I think it is important also to look at the rate of denial to eligible applicants.

Mr. SHAW. But you want a separate statistic; you are taking issue that it should not be counted together as one net figure?

Ms. SMITH. No, I wouldn't take issue with that.

Mr. MILLER. Could I add something to that?

Mr. SHAW. It sounded to me like that was your testimony.

Mr. MILLER. Underpayments is not a question of taking credit. Underpayments becomes another ground of sanction. So I think what we are saying here is that the States themselves would be willing to have a system that penalizes underpayments as well as overpayments, and in the context of a broader system that over all is fair and equitable and only measured mistakes and not what the present system does.

Mr. SHAW. Then you agree that in determining the State's liability we should give States credit for underpayments?

Mr. MILLER. We should take underpayment into account in determining the State's liability, yes, but that is not a credit. It is another penalty.

Mr. SHAW. I understand.

Thank you.

Acting Chairman DOWNEY. Mr. Pease.

Mr. PEASE. One question. I appreciate the testimony of the panel.

I read the testimony of the Assistant Acting Secretary, and you mentioned in your testimony that the administration will soon propose a three-tiered carrot and stick approach. I wondered if any of our current panelists commented in their testimony on the administration's proposal, and if not, if you would like an opportunity to do so.

Mr. MILLER. Mr. Greenstein did have some considerable comment about the administration proposal.

For what it is worth, I would like to add that any proposal that bases sanctions solely on the numbers produced by the sample-based system, in our view, is a seriously flawed system.

What the administration proposal does is to modify the numbers within the present system, but still ends up with what is the core, I think, failing in that a penalty is predicated upon the results of a very rough sample-based statistical methodology and not based upon some intelligent, rational analysis of whether the States actually administered their program in such a bad way it deserved to be penalized.

Ms. SMITH. In addition to the concerns just raised by Mr. Miller, I think the other concern that the Governors have about the administration proposal is the notion of prospective collections.

The idea that a State would be penalized in advance of potentially making any errors to us is an issue of great concern. That takes the money away from the States before they have even had an opportunity to show that they have done a good job.

Mr. SHAW. Would the gentleman yield?

Just a follow-up question to any of the witnesses. How do we account for such a wide dispersion in error rates across the States? Is part of the difference in error rates caused by incompetence or an attitude within the various States about how responsible they should be in making proper checks and ensuring that things are done correctly?

Ms. SMITH. Mr. Shaw, I think that there isn't a State in the country that isn't concerned with running a good program. We put at least on average 50 percent of the money into this program, and it is no fun for a governor to wake up in the morning and see in the headlines that his State has gotten another letter from HHS and he has another $100 million in fiscal sanctions.

So I think it is important to note that without a single dime in fiscal sanctions being collected, over the course of the years the States have brought the error rate down from 16½ to 6 percent. I think some of the variation has to do with the fact that some States are more automated than others.

States have different kinds of caseloads and different kinds of programs. The AFDC program doesn't look the same in every State. If you have States that run a program supplying benefits to two parents as well as single-parent families, you have a different kind of calculation to make. So that to some extent, the differential in the errors has to do with the modernization of the State and its ability to keep enough eligibility workers on hand to make careful determinations, and I think it depends on what the program looks like.

But all States have brought their error rates down dramatically without the imposition of any fiscal sanctions in the last few years.

Mr. GREENSTEIN. There is a combination of factors that are beyond the State's control that could account for differences and factors that are within State control.

On the factors beyond their control, as several of the panel members mentioned, the composition of the State caseload is important.

An HHS study issued in 1986 found that the AFDC error rate is nearly three times as high among families with earnings as without. Therefore, a State that has a much higher proportion of its caseload consisting of families with earnings with an equal measure of performance would still end up with a higher error rate.

Similarly, the study found that a typical urban area was expected to have an error rate about 3 percentage points above the predicted national average rate. So there are certain factors there that really sort of were baked into the cake before you start.

Second, there are these technical or nondollar areas we have referred to. I don't know if this has been done. What would be interesting would be to remove from each State's error rate the nondollar errors and then to make an appropriate adjustment for differ-

ences in the caseload, urbanization, earnings and so forth, and then see what the variations would look like. That is the sort of thing the Matsui or Moynihan bills do for levying sanctions.

After that is done, those States that are still the highest error rates should, in my view, be subject to a potential fiscal sanction. That is the way I think we ought to reform the system, is take account of the factors that are beyond their control or that aren't really errors, and when you have done that, isolate the group of States that have the worst performance and go after them appropriately.

The other thing I would say is I don't know if there is legal authority needed or not, but if there is, I think the subcommittee might want to look at giving HHS additional legal authority in another area.

In the Food Stamp Program, there is another sanction authority whereby without regard to these automatic dollar QC errors, if a State is deficient in a particular area of administration, the Department may warn the State; and if the deficiency isn't corrected, proceed to suspend or withhold a portion of the State's administration funds.

On the issue of technical errors, if a State is not collecting Social Security numbers as it should—I am not suggesting that we ignore that. If that is the case in the Food Stamp Program, the Department would move towards an administrative sanction unless the State corrected it, and if the State corrected it, it wouldn't have to impose sanctions.

One of the problems with the QC is it sort of substitutes for the other compliance tools that HHS might have to improve performance among States that are performing below average.

Acting Chairman DOWNEY. I thank the panel for an interesting discussion.

The committee will next hear from its second panel: Michigan Welfare Rights Organization, Adele Blong, Center on Social Welfare Policy and Law; Connecticut Department of Income Maintenance, Patricia Day, director of management planning and evaluation; Texas Department of Human Services, Rex Downing, administrator, Quality Control Division; California Department of Social Services, Leslie Frye, chief, Policy Implementation Bureau; Colorado Department of Social Services, Bonnie Orkow, director, Division of Quality Assurance.

Mr. MATSUI [presiding]. I want to thank all members of the panel for attending this hearing today.

As the panel can see, other members have other matters that they have to attend to at this time. We are going to try to limit everybody to 5 minutes and try to proceed as rapidly as possible.

I would like to call now the first witness from the Michigan Welfare Rights Organizations, Ms. Blong.

STATEMENT OF ADELE M. BLONG, CENTER ON SOCIAL WELFARE POLICY AND LAW, MICHIGAN WELFARE RIGHTS ORGANIZATION AND HOUSTON WELFARE RIGHTS ORGANIZATION

Ms. BLONG. Good afternoon. We are happy to be here to participate in hopefully what will be the first step to achievement in this

Congress of a reasonable and realistic quality control system that will be fair to the States, fair to the Federal Government, and fair to the program beneficiaries.

To answer what may seem a question, why are we here in the midst of what seems a technical debate between the States and the Federal Government over fiscal and statistical questions, we are here because ultimately it is poor families who will bear the brunt of disallowances that are collected for past years or sanctions imposed in the future.

Clearly, if the Federal matching is reduced, States will have to respond to adjust their State expenditures, and unfortunately the most likely adjustment will come in the form of AFDC benefit levels, thus reducing the aid available to poor families in the State.

In addition, even at the current time, it is poor families in the States who bear the brunt of current State policies and procedures that overreach as a result of State fear of fiscal sanctions, the types of things that we have referred to in our prepared statement as excessive verification requirements.

We would submit that the purpose of quality control is to ensure that public assistance goes to the poor families who meet eligibility standards as well as concerns about payments to ineligibles, that in order to meet this standard the system must measure the correctness of all decisions made under federally approved procedures to determine whether or not States are performing against their own procedures; that it is equally important and perhaps more important that the system measure whether proper performance under those procedures is nonetheless resulting in denial of aid to families that are eligible, in other words, whether or not the procedures themselves are screening out eligible families. The purpose of the latter being to determine, if that is done, are there ways that those procedures can be improved consistent with concerns over fiscal accuracy and also consistent with the goal of assuring that needy families receive the aid for which they are eligible.

The primary purpose of this program should be identification and correction of errors, not a punitive fiscal sanction for the errors that exist, should some goal of improving the program rather than simply looking at the past.

We don't necessarily suggest that any of these errors should be the subject of sanctions, and have serious questions as to whether or not in the long run that is an appropriate way to improve program performance. But certainly if sanctions are to be imposed, they should be even-handed and should look at all errors in the program and not just overpayment errors.

They should look at underpayments, erroneous denials and erroneous terminations. In addition, the program should look at issues like whether or not so-called proper denials and proper terminations are nonetheless screening out aid to eligibles and in the second case, not for purposes of sanctions, but for purposes of identifying appropriate corrective action plans.

I think the need for this is illustrated by the dramatic increase in denials after the onset of the fiscal sanctions programs. From the year 1972, the year prior to fiscal sanctions, until 1984, denials increased by more than 1 million a year in the AFDC Program. In the year 1984, 3.2 million of the reported denials were reported to

be procedural denials, cases in which families were denied not because they were found to be ineligible, but on the theory that they had not complied with some documentation requirement.

The mere fact of such an extreme number would suggest a critical need to scrutinize what is going on there. Studies show that there is substantial reason to think that many of those procedural denials are, in fact, denials to ineligibles.

I would like to mention on the collection of the disallowances that families, poor families will pay. I would also offer that collecting the disallowances at this point has no corrective effect. There is no way in which they can stimulate a State response, a cure. States have been acting over the intervening years on the basis of the statistics as to their error rates in order to affect those error rates, and the disallowance now is simply a fiscal penalty with no other purpose.

Also, while HHS questions whether or not the system is flawed, I think they have implicitly admitted it. After 8 years of experience under a program that started with a 3-percent error rate when States were far above that rate and have dropped down over the years, HHS now suggests that prospectively a 6-percent error rate is appropriate. I think that is an admission that the 3-percent error rate was wrong from the beginning and is wrong now.

Mr. MATSUI. Thank you.

[The statement of Ms. Blong follows:]

THE AFDC QUALITY CONTROL REFORMS RECOMMENDED BY THE NATIONAL ACADEMY OF SCIENCES SHOULD BE ADOPTED

Statement prepared for presentation before the Subcommittee on Human Resources of the House Committee on Ways and Means, May 8, 1989

By

Adele M. Blong
Timothy J. Casey
Mary R. Mannix
Center on Social Welfare Policy and Law
1029 Vermont Avenue, N.W.
Washington, DC 20005
(202) 347-5615

On behalf of

Houston Welfare Rights Organization
and
Michigan Welfare Rights Organization

Statement

We appreciate the opportunity to appear before the Subcommittee today on behalf of the Houston Welfare Rights Organization and the Michigan Welfare Rights Organization. Both organizations have fought for many years against the one-sided focus on overpayments Quality Control has had since 1973 and for a non-punitive QC system which will promote quality administration. QC's one-sided overpayment focus causes widespread denials to eligibles and its punitive sanctions threaten additional grave harm to the needy children AFDC is supposed to help.

Originally, Quality Control's sole purpose was to measure error so that program managers would have the information needed to decide if corrective action was warranted. In 1973 the federal AFDC agency gave Quality Control the second purpose of sanctioning "excessive" overpayments, an action that Congress in effect ratified some years later by adding an overpayment sanction policy to the statute. While the QC sanction policy is usually at the center of "reform" discussions, QC measurement policies mask the fact that denials to eligibles are much more common than payments to ineligibles and true reform must address this issue as well.

As the Subcommittee knows, last year the National Academy of Sciences recommended a new QC system. It did so after concluding from an exhaustive two year study that the current system does not promote quality administration. From Quality Control to Quality Improvement in AFDC and Medicaid, (Washington, D.C.: National Academy Press, 1988). HWRO and MWRO supported the Academy's recommendations in their testimony before the Subcommittee on April 12, 1988 and again do so today.

The Academy stated that its reform recommendations were intended as a package, recognizing the danger that true reform could be defeated by a process in which

different groups sought enactment only of those recommendations which they deemed to favor their interest. (Academy Report, p. 209). As a package the Academy's recommendations are fair to the federal government, fair to the states, and fair to the poor families AFDC is intended to benefit. As a package they should set the framework for a new QC system which will promote quality administration. Unlike the current system, this new system would define "excessive" error realistically, treat unauthorized denials and unauthorized payments evenhandedly, measure the number of denials to eligibles as well as the number of payments to ineligibles, hold states accountable for compliance with authorized program procedures but not for the procedures' less than perfect results, and require federal AFDC officials to improve program procedures if they can be improved.

Two major obstacles stand in the way of the new QC system the Academy recommended - the sanction backlog and the federal AFDC agency's excessive focus on overpayments and sanctions. Federal AFDC officials have for years treated the federal interest in state AFDC administration as being to reduce overpayments and to maximize the number of states which are sanctioned for supposedly excessive overpayments. See T. Casey and M. Mannix, Quality Control in Public Assistance: Victimizing the Poor Through One-sided Accountability, 22 Clearinghouse Review 1[illegible]-1389 (April 1989). This is a too narrow and punitive definition of the federal government's interest. The federal government also has an interest in reducing denials to eligibles, and sanctions can not improve performance unless they are carefully tailored and sparingly used.

The Sanction Backlog Should Be Forgiven

The states have accrued an outstanding sanction liability exceeding $1 billion under current sanction policy. The "sanction backlog" must be resolved quickly and fairly. Until it is fairly resolved, federal and state AFDC officials will not turn their energies to building a better QC system. They will spend years in the courts battling over the backlog if the collection moratorium expires on July 1 and the issue has not been resolved. As the Academy's report gives the states so much ammunition, they have no reason to give up the fight.

The Academy found the QC policies which have produced the backlog to be unsound, unjustified, unrealistic and unfair. If the backlog is collected states will pay it by cutting benefits or administration or both. Given the Academy's findings and the harm to the program's beneficiaries and the quality of administration if the backlog is collected, the fair and sensible thing to do would be to forgive the backlog. If this is not politic, the backlog should be resolved by what the Academy called the "solution of expedience" of collecting sanctions only from states whose backlog period overpayment rates were extremely high in relation to the distribution of state rates. This is the approach taken by the Senate QC reform bill which Senator Evans, now retired, introduced last year, and which Senator Moynihan has reintroduced as S. 231 this year.

States Should Be Held Accountable For Compliance With Federally Approved Verification Procedures But Not For Those Procedures Less Than Perfect Results.

Since adopting an overpayment sanction policy in 1973 the federal AFDC agency has encouraged denials to eligibles by its overbroad QC definition of a payment "error". It charges states with "errors" for payments to families whose ineligibility is not detected by the federally authorized program verification procedures. This policy drives states to adopt extreme verification requirements whose main effect is to cause denials to eligibles. The Center verification study which the Academy repeatedly cited concluded that denials to eligible families for "failure to verify" had tripled since 1973 and now exceed a million a year. (This study, Quality Control and the "Churning" Crisis, is reprinted in the transcript of the October 22, 1987 joint Senate and House Agriculture Committee hearing on Quality Control And Fiscal Sanctions In The Food Stamp Program, and was furnished to the Subcommittee with our 1988 testimony.) A 1988 study for the Southern Governors' Association also identified the growth in such denials due to the QC sanction policy as a major program problem. Shuptrine, S. and Grant, V., Study of the AFDC/Medicaid Eligibility Process in the Southern States. (Washington, D.C.: Southern Governors' Association, 1988).

QC should continue, as the Academy recommended, to measure all overpayments. However, as the Academy also recommended, QC should define as "errors" only overpayments due to failure to follow the federally authorized program procedures. If a state has followed the authorized procedures and an overpayment nevertheless occurs, the state should not be charged with an "error".

It is inevitable that program verification procedures will sometimes fail to detect ineligibility. The federal government can fairly hold states accountable for compliance with the authorized program verification procedures but not for the fact that the procedures do not have perfect results. If the procedures can be improved, federal officials should improve them and use QC to hold states accountable for compliance with the improved procedures. If program procedures can not be improved, states should not be blamed for this.

QC Should Measure The Number Of Authorized Denials To Eligibles For Failure To Satisfy Verification Requirements And Should Improve Its Procedures For Measuring Unauthorized Denials.

A recent GAO report described the following incident. In March 1985 a county Food Stamp office denied Food Stamp recertification to a woman with three children for failing to supply verification of how much child support the county Child Support Enforcement office was collecting for her. On her March recertification application she reported the same $40 bi-weekly amount she had documented three months earlier and gave the Food Stamp office her child support enforcement case number so it could verify she was still receiving the same amount. The Food Stamp office nevertheless denied the recertification application. In June she reapplied and was accepted. September 1985 documentation in her case file indicated she was still receiving the $40 bi-weekly in child support she had reported. Food Stamp Program: Administrative Hindrances to Participation, GAO/RCED-89-4 (October 1988); Letter from John Harman, Director, Food and Agriculture Issues, GAO, to Timothy J. Casey, Center on Social Welfare Policy and Law (March 13, 1989).

QC selected the March recertification application denial for QC denial review. Using the same policies used in AFDC QC denial review, QC found that the denial was authorized. Program verification rules required the woman to verify the reported child support amount and she had not done this. While the Food Stamp Office could have contacted the child support office to verify her report, program rules did not require it to do so.

QC did not investigate whether the denial, although authorized by program verification rules, was a denial to an eligible. Under current AFDC and Food Stamp denial review rules, QC does not investigate whether authorized denials for failing to comply with verification requirements are denials to eligibles.

Due to the verification extremism spawned by QC's overbroad definition of a payment "error", failure-to-verify denials now account for about half of all AFDC denials. QC finds almost all to be authorized and, due to the limited scope of QC denial review, no one knows for certain how many are denials to eligibles. Our estimate from the available data is that two thirds or more are denials to eligibles. Many verification denials to eligibles could be avoided by inexpensive changes in program verification rules which would not increase payments to ineligibles.

S. 231 would require QC to measure whether authorized verification denials are denials to eligibles. This is an essential reform since program managers must have this information to evaluate the consequences of current verification rules. S. 231 would not define authorized verification denials to eligibles as errors. This is consistent with the Academy's recommendation that overpayments not be defined as errors if the authorized program verification procedures have been followed.

The second problem with QC denial review is that the reported rates of unauthorized denials are almost certainly below the true rates. Food Stamp denial review rules are modelled on the AFDC rules. GAO recently found the reported Food Stamp rates to be far below the true rates. Food Stamp Program: Evaluation of Improper Denial or Termination Rates, GAO/RCED-88-12 (October 22, 1987). To solve this problem denial review procedures must be redesigned to include field investigations and federal validation of state findings. These essential accuracy safeguards have been included in the QC payment review process for over a decade.

If QC denial review is improved so that it measures authorized denials to eligibles and accurately measures unauthorized denials, the results will reveal that denials to eligibles are probably 10 to 20 times as common as they are usually thought to be based on the rates of unauthorized denials now reported by QC. The federal government should assure the states they will not be singled out for the blame since it is the federal QC sanction policy which is principally responsible for the problem.

The Sanction Policy Should Be Evenhanded

Sanctioning overpayments but not underpayments and unauthorized denials sends the message that avoiding

underpayments and erroneous denials is not a priority. This message inevitably causes underpayments and denials to eligibles. Because a one-sided policy sends the wrong message the Academy recommended the evenhanded policy of also defining underpayments and unauthorized denials as potentially sanctionable error. The General Accounting Office (GAO) likewise recommended this be considered after finding shockingly high Food Stamp unauthorized denial rates in some states. Food Stamp Program: Evaluation of Improper Denial or Termination Rates, GAO/RCED-88-12 (October 22, 1987).

The Administration's Proposals Are Inconsistent With The Academy's Recommendations

The Administration's proposals ignore the Academy's recommendations for a redefinition of sanctionable payment "error", an even-handed sanction policy, and improved QC denial review. They would make QC even less even-handed by rewarding states with very low payment error rates without regard to their denial error rates and with no rewards for very low denial error rates. They also embody a "sanction first and sanction as many as possible" approach which is punitive, harmful, and counterproductive and inconsistent with both the letter and spirit of the Academy's recommendations.

The Administration proposes to go beyond current law by "prospectively" collecting sanctions based on guesswork before state error rates are even known and before states with "excessive" errors are allowed to seek the sanction waiver provided by current law. This is inconsistent with basic due process principles. Sanctions should not be collected until an error rate has been determined, any waiver request has been fairly considered, and there has been an opportunity for a full and fair review of the state's liability. The Academy found that the current procedures for challenging federal error findings are deficient and cautioned that due process protections must be observed. (Academy Report at 225-226)

The prospective collection proposal also fails to recognize that sanctions should be the last resort not the first response to excessive error, as states are likely to absorb a sanction by cutting benefits and/or administration. Sanctions should be imposed only when a state will not take corrective action to reduce excessive error. This is basically the approach taken by S. 231 and is the approach Congress has adopted under §403(h) of the Social Security Act for deficient state performance in collecting child support.

Standards for defining "excessive" error should be realistic. The Academy found the 97% payment accuracy standard implicitly set by the current 3% payment error tolerance level to be highly unrealistic. The Administration makes a limited concession to this finding by proposing to substitute a 94% standard which would gradually be increased to 94.5%.

A 94% standard is itself unrealistic. Twenty-six states had a payment accuracy rate less than 94% in either 1985 or 1986 or both. There is no evidence this resulted from lack of effort to do better. Improving payment accuracy has been the states' overriding administrative goal for more than a decade and states have spent huge sums

trying to do so. If after a decade of sustained effort many states do not achieve a 94% rate the obvious conclusion is that many do not have the capacity to achieve it.

The Academy recommended treating as having "excessive" overpayments only states whose payment accuracy rate is substantially below average. This is an eminently reasonable proposal given that the average payment accuracy rate has been virtually constant throughout the 1980's despite huge expenditures to try to improve payment accuracy. From 1981 to 1986 the national payment accuracy rate fluctuated in the narrow range of 92% to 94% with the average state rate only slightly higher.

Based on the most recent available data, all states seem capable of achieving a payment accuracy rate within 5 percentage points of the average state rate, about 95% in FY 1986, although some states do not always do so. It might therefore be reasonable to use a "more than 5 percentage points below the average" rule to identify states with "excessively" low payment accuracy rates. Federal agency officials should aid such states to develop a reasonable corrective action plan. Sanctions could then be imposed if a state refused to implement the plan. The same approach should govern if a sanction policy is extended to underpayments and denials to eligibles, as it should be if there continues to an overpayment sanction policy.

Mr. MATSUI. Your written testimony will be inserted in the record.

STATEMENT OF PATRICIA DAY, DIRECTOR OF MANAGEMENT PLANNING AND EVALUATION, CONNECTICUT DEPARTMENT OF INCOME MAINTENANCE, AND ON BEHALF OF THE AMERICAN PUBLIC WELFARE ASSOCIATION

Ms. DAY. I would like to share a different perspective, one I bring as a former teacher, because I am fascinated by the analogies to the education system that Chairman Downey had mentioned. These first occur as you see that the 3-percent tolerance level stood on its head is really a 97-percent accuracy rate, and 97 translates into an A-plus in school.

The problem is that this is not a target; this is the passing grade. If you get A-plus, you pass. Everybody else flunks—the A's, the B's, the gentlemen's C's.

When you apply the system, all but one State flunked between 1981 and 1986. If a school had flunked all but one student, it would be the school that would be called into question, not the failing students. After all, the school is the one that decides what the students are to accomplish, how they are to be measured and what is to be the passing score and consequences. When we start with what is to be accomplished by States, Congress wants us to deliver benefits and services accurately to eligible recipients, and that is fine.

The problem arises when Congress mandates the means to those ends and that is what these technical issues are: means. It was thought by some that requiring certain technical processes like registration for WIN and monthly reporting would help us meet our ends. But when those requirements were enacted and QC reviewers started looking at them for errors, we started being penalized for accurate cases—even though they were perfectly correct—we just didn't get the technical processes done.

In the school analogy, it is as if the school decided that doing extra book reports would help the students learn their lessons, and then flunked students who knew their lessons perfectly just because they didn't get all their book reports finished.

How have these technical requirements affected error rates? In chart A you can see that in Connecticut, for 1988 we have 1½ percentage points in technical error. That is $1.5 million in sanctions due to technical error, mostly monthly reporting. Connecticut is ahead of nearly everyone in terms of the jobs program. This may be foreshadowing what is to come for the whole country. As we put more people to work, we are exposing ourselves to higher error rates.

Chart B, shows that technical errors have doubled Connecticut's sanction liability in the last 8 years. It was $4 million; with the technical error, it is $8 million.

The problem is that monthly reporting just doesn't work. It seemed like a good idea at the time, but it doesn't work. It creates technical errors and makes workers so busy trying to take care of these technical requirements that they actually make real errors.

We are in a real double bind. At the same time Congress adds the new work requirements, they start bringing the error rate tar-

gets down. It is like the teacher giving us extra book reports and then raising the passing score so that we are caught in the middle.

This is one of the reasons that we think that some variation on the national average is a good target, because it self-adjusts for new responsibilities added by Congress. Those can be reflected in the changing rates over time. The national average also helps to give recognition to new challenges that come about due to economic and demographic change.

There are many other problems with the system which NAS has pointed out. I'll just mention a couple that fit with our analogy. We have common goals in AFDC and the school system. We want to create people who are as self-sufficient as possible out in the world. There are many steps to that goal, but our system has a very narrow focus; it just measures payment accuracy and all of the rest is ignored. As a result, the sanctions cause us to focus State resources on payment accuracy. It's as if our student had to spend all his time studying for true-false exams, and didn't have time for any of the broader academic experiences that create productive citizens. We can't run a good program that carries out the Family Support Act if we are constantly worried about these sanctions and focusing solely on payment accuracy.

Another problem with the system is that it is based on sample data. We sample cases in QC and the teacher samples facts, because you can't look at everything. Since there's a margin of error in how well the samples represent the whole, you need a margin of uncertainty to interpret the results.

They handle this in school by grading on the curve. We are suggesting that what is in Mr. Matsui's bill as a way to handle the retrospective sanctions takes care of this problem. It would be good for handling prospective sanctions as well. We have chart D that shows how in a school system, you grade on a curve. A-pluses can be relieved from requirements, A's, B's, and C's continue to do plans, and C-minus and back should be looked at again very carefully. Chart E shows how this same approach would work in our QC system.

The worst part with the sanctions is that it diverts resources from our program goals. It is as if the school identified a student who was having trouble passing and then decided to make him wash out the school buses all day. It doesn't help the student at all; it just punishes the student and helps the school budget a little bit. That is what the sanction system is doing to us. When the system forces us to jump through technical hoops and spend our energies defending against sanctions and then takes our money away, we don't have the time and resources to attend to what you want us to do.

As a last point with the school analogy, I'd like to address the bizarre notion of prospective sanctions. They can only be likened to something akin to "advance flunking."

For all the reasons above, we feel it is important that we get a new QC system that doesn't penalize us for technical errors, that creates a way to identify extremes for special attention, and that looks at sanctions as a last resort, not as a source of Federal funds.

Mr. MATSUI. Thank you.

[The statement of Ms. Day follows:]

TESTIMONY OF PATRICIA DAY
DIRECTOR, MANAGEMENT PLANNING AND EVALUATION
CONNECTICUT DEPARTMENT OF INCOME MAINTENANCE

Thank you, Mr. Chairman. I am Patricia Day, Director of Management Planning and Evaluation in Connecticut's Department of Income Maintenance. I chaired the American Public Welfare Association's Task Force on Alternative Quality Control Systems, and I served on the workgroup that forged a joint quality control policy statement for the National Governors' Association and the National Council of State Human Service Administrators. I am pleased to be here to testify on behalf of Connecticut and the American Public Welfare Association.

Later on I have specific responses to the questions posed in your announcement of the hearing, but first I would like to share with you some of the general problems states face with the current AFDC Quality Control system. As a former teacher I am fascinated with the analogies to a school grading situation. This first comes to mind when one sees the AFDC 3% tolerance level as a requirement for 97% accuracy -- a level that translates in school to A+ performance. This A+ level is not just a target, though; it's the passing grade. If you don't get 97% -- the A+ -- you flunk. There's no middle ground. The A+ passes; everyone else flunks: the A's, the B's, and the gentleman's C's. Now how does this approach work out in practice? For the years 1981 through 1986 the system flunked every single state except Nevada at least once. Only four states have been able to achieve the 97% for more than one year.

If a school flunked all but one student it would be the school, not the failing students, that would be called into question. After all, it's the school (and in our case the federal government) that decides on the three broad features of the system: 1) what the students (states) must accomplish, 2) how the performance is to be measured and 3) what the passing score and consequences will be. There's obviously something wrong with our system; and I suggest to you that there are problems in each of these three features.

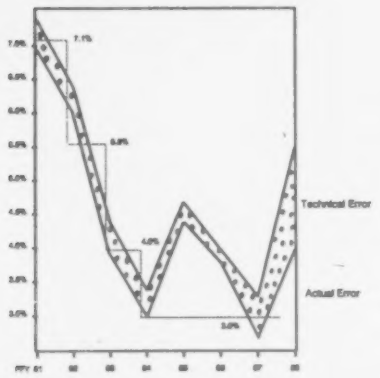
WHAT IS TO BE ACCOMPLISHED BY STUDENTS (STATES)

Just as the school decides what students are to accomplish, Congress decides what states are to accomplish in the AFDC program: delivering the appropriate services and benefits to truly needy recipients based on specific and very complex eligibility tests. This is fine. The problem arises when technical requirements are added to our curriculum, and then those means are confused with ends. It was thought that performing certain technical processes would be a **means** for achieving accurate benefits and eligibility determinations; these technical processes included registering recipients for work, getting SSN's for all family members, and requiring monthly reporting for recipients with earnings. Once these processes were enacted as part of our requirements, the federal QC system began reviewing them for errors. Now, if a state has achieved its **ends**, a correct benefit to an eligible case, it can still be penalized for the case's entire benefit amount if the technical processes -- the prescribed **means** -- weren't carried out.

It's just as if the school decided that doing extra book reports in every subject would help students learn their lessons, and then flunked students who knew the lessons perfectly but didn't finish all their book reports. Let's see how adding these technical requirements (and the potential for technical error) has actually affected our rates. Chart A shows Connecticut's actual error and the additional technical error for years FFY81-88 (estimated). The bulk of our technical error is due to monthly reporting, a fairly new process whose effects don't show up in the QC system until after FFY85. The increase in technical error is directly attributable to the monthly reporting requirement; the increase in actual error is also partially due to it. When

CONNECTICUT ERROR RATES
DUE TO ACTUAL VS. TECHNICAL ERROR

Chart A

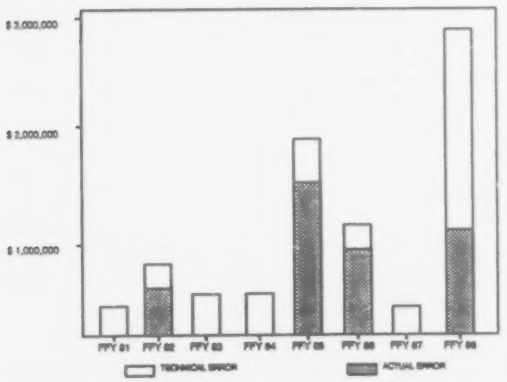


	ACTUAL ERROR	TECHNICAL ERROR	TOTAL ERROR
FFY 81	6.9%	0.5%	7.4%
FFY 82	6.0%	0.4%	6.4%
FFY 83	3.9%	0.5%	4.4%
FFY 84	3.0%	0.4%	3.4%
FFY 85	4.4%	0.3%	4.7%
FFY 86	3.8%	0.2%	4.0%*
FFY 87	2.7%	0.6%	3.3%*
FFY 88	4.0%	1.5%	5.5%*

* Estimated
Note: Impact on regressed error rate for technical and actual errors is estimated.

TECHNICAL ("PAPER") ERROR DOUBLES
CONNECTICUT'S SANCTION AMOUNTS!

Chart B



	SANCTION DUE TO ACTUAL ERROR	SANCTION DUE TO TECHNICAL ERROR	TOTAL SANCTION AMOUNT
FFY 81	-	$ 313,000	$ 313,000
FFY 82	$ 500,000	$ 354,235	$ 854,235
FFY 83	-	$ 435,911	$ 435,911
FFY 84	-	$ 440,258*	$ 440,258*
FFY 85	$ 1,600,000	$ 314,786	$ 1,914,786
FFY 86	$ 900,000	$ 200,000	$ 1,100,000**
FFY 87	-	$ 300,000	$ 300,000**
FFY 88	$ 1,100,000	$ 1,600,000	$ 2,700,000**
TOTAL	$ 4,100,000	$ 3,958,190	$ 8,058,190

* Question waiver request was approved.
** Question amounts estimated.
Note: Impact on regressed error rate for technical and actual errors is estimated.

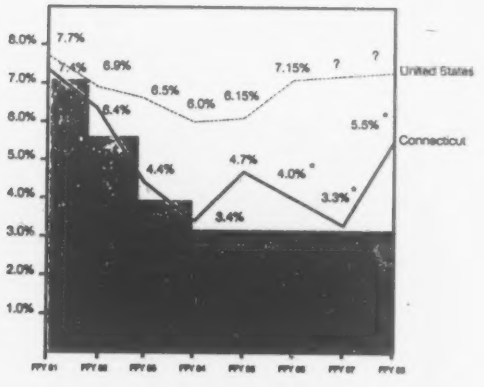
workers must spend their limited time doing extra technical paperwork it complicates their job and leaves less time for the real tasks and greatly increases the potential for real error. So a technical process instituted as a means to better performance has backfired. First, it hasn't been effective in reducing error (bearing out the results of earlier demonstration projects); second, it has increased error rates by creating the potential for new technical error and the probability of new actual error; and thirdly, it has created new sanction liability for states that penalizes them for accurate cases. Chart B shows how these technical errors doubled Connecticut's liability. The bad part is that the average observer sees these figures and assumes we could have saved the $4 million by correcting these "errors", when in fact the cases are most likely already correct and no money can be saved. The worst part is that the real sanctions for these technical paper errors make it even more difficult for us to achieve our true ends: delivering services and benefits to eligible recipients. They may even lead us to spend real dollars to correct paper errors to avoid real sanctions -- a result we're sure Congress didn't intend.

Is Connecticut alone in this situation? A look at Chart C shows a similar pattern for Connecticut and the U.S. as a whole. We had reached an all-time low in 1984, and since monthly reporting was instituted we see an increase throughout the country.

Chart C also demonstrates the double bind that states have been caught in by the current system. At the same time Congress began adding requirements which increased error proneness and therefore error, it lowered the sanction tolerance level. In our school analogy, the teacher started loading us with the extra book reports and then raised the passing grade! In 1981 the passing score was 92.9%; it moved to 94.5% in 1982, to 96% in 1983, and to 97% in 1984. If either aspect had remained stable we would have fared better. Had the tolerance levels stayed at 1981 levels, we would have avoided sanctions from 1982 on; or had technical errors been removed we could have avoided sanctions for four of the eight years. But with both forces together we exceeded targets every single year in this no-win situation.

CONNECTICUT ERROR RATE
COMPARED TO THE U.S. ERROR RATE

Chart C



* Estimated
Note: Federally-computed error rates

It is clear that the demands on the states and the passing scores are interdependent functions which should be considered together when changes are made. Here we've been discussing technical requirement changes which are particularly frustrating to the states. But there will always be real program changes (changes to the basic curriculum) that Congress needs to make. It is vital that error targets are adjusted to reflect such increases in real responsibilities. Otherwise, we'll arrive again at today's situation: targets that are so impossible, they become irritants instead of incentives. This is one reason why some variation on the national average makes an ideal target -- it self-adjusts for new responsibilities added by Congress, as well as for new challenges brought on by economic and demographic change.

HOW PERFORMANCE IS TO BE MEASURED

The many flaws in the current AFDC QC measurement system have been thoroughly reviewed and documented by the National Academy of Sciences in their Congressionally-mandated study. I will just go over a couple which fit with our analogy. The school and our AFDC system actually have similar end goals: to help individuals become as fully self-sufficient as possible out in the world. There are many steps and processes in meeting these goals, but we have a QC measurement system that focuses in narrowly on just payment accuracy. When sanctions are attached to this focus, so are state resources-to the detriment of program objectives which lead to long-term self sufficiency goals. It's as if our student must spend every minute studying for true-false exams and has no time left for the broader academic experiences that grow him into a productive citizen. By its passage of the Family Support Act, Congress clearly has broad goals for the states in managing the AFDC program. It is critical that progress toward them not be hampered by a performance measurement approach that gives undue weight to just one performance indicator.

Another problematic aspect of the measurement system is the fact that it is based on sample data. The QC system can't look at every case in the country; it looks at samples. The school can't test for every fact the students are to learn, so it tests for a sample of facts. The problem is that the particular samples chosen may not reflect the true knowledge of the student or the true accuracy of a state's caseload. To account for this margin of error regarding which sample cases are chosen, there needs to be some margin of uncertainty used in interpreting sample results. States have proposed using the statistical concept of a confidence interval and counting error at the lower end of this range to protect against the "sampling error" mentioned above. In school a teacher may account for this uncertainty by "grading on the curve" and doing more testing on those who don't do as well as the larger group. As will be discussed below this school approach would be an acceptable alternative to states if confidence intervals are seen as too complicated.

WHAT THE PASSING SCORE & CONSEQUENCES SHOULD BE

As we are hearing today, impossible targets are useless targets. They demoralize the students and they can't be enforced as standards. Just as the school board, when appealed to, wouldn't stand behind a teacher who flunked all but one student; neither would the court, when appealed to, be able to justify a sanction system that flunked every state but one. We need a new set of targets and a new set of consequences. Although we support the approach laid out in the Moynihan bill, I'd like to elaborate here on the "school" alternative which is basically the two-step process the states are proposing for the backlog resolution (see amendment proposal below). What I suggest to you is that it is also a good approach for the future system.

Chart D shows the school version; Chart E shows the proposed QC version.

SCHOOL APPROACH

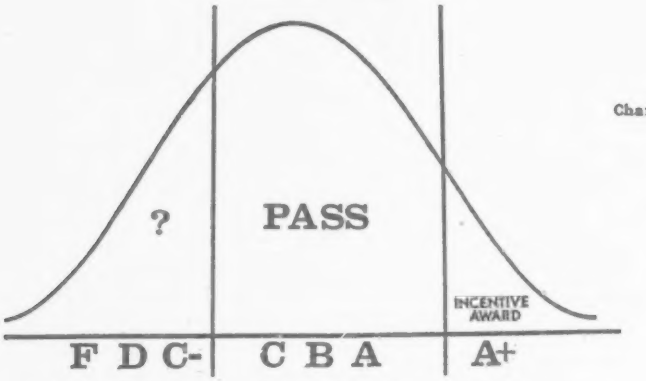


Chart D

- individual examination to determine actual knowledge
- individual consideration of any special problems or challenges
- evaluation of student's ability to achieve and effort to achieve
- special tutoring if needed
- offer to pass if student agrees to put in extra effort (summer school)
- Flunk only as a last resort

- continue homework with focus on individual problem areas

- waive all homework

PROPOSED

QC APPROACH

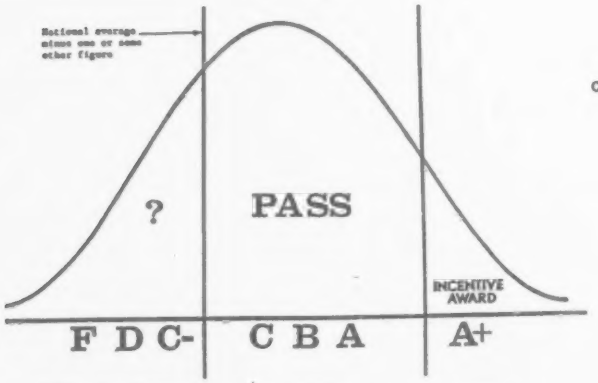


Chart E

- individual state examination to determine actual, avoidable error
- individual state consideration of any special problems or challenges
- evaluation of state's ability to control error and its effort to control error
- special technical assistance if needed
- offer to pass if state agrees to put in extra effort (channeling more state funds into administrative costs to reduce errors).
- sanction only as a last resort

- continue requiring quality improvement plans with focus on individual problem areas

- waive quality improvement plan requirements

In both these examples, "grading on the curve" interprets the raw scores in a way that adjusts for the difficulty of the work -- comparing individual performance to the group distribution. Both approaches identify a threshold score, above which individuals receive a routine treatment, and below which individuals require further examination before a final determination can be made. This proposal for a QC approach has several advantages: 1) it conforms to recommendations of the National Academy of Sciences; 2) it reduces the incredible federal and state administrative burdens involved in elaborate waiver processes for states that are actually performing well; 3) it thereby allows for targeting federal resources on states that more likely do need special attention and assistance; 4) it is a fair and equitable approach which emphasizes quality improvement, but also identifies for closer scrutiny those states that might actually warrant sanctions; and 5) it reduces the number and amount of sanctions which most often are counterproductive.

The counterproductive nature of sanctions is partly due to the failure to recognize the point of diminishing returns in reducing errors.

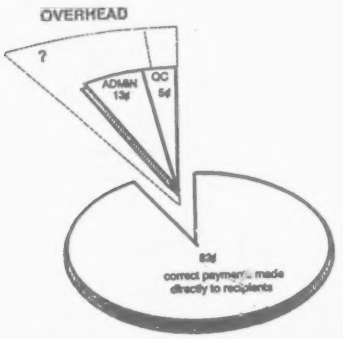


Chart F

Chart F shows that in FFY '88 Connecticut was able to deliver 82¢ of each dollar of total expenditures directly and correctly to recipients. The 13¢ of administrative cost and 5¢ of QC error cost are part of overhead. It's important to see the errors as a cost of doing business. If necessary, they can be reduced, but now that our "big bang" improvements have been made, most of the easy error reductions are already achieved. Connecticut reduced its rate from 9.7% in 1979 to 3.4% in 1984.

Further error reductions will be difficult and expensive and may not be cost-effective. If we spend excess administrative funds to achieve a very low error, we will either increase our total expenditures or cut into our 82c direct delivery and thereby disadvantage our program recipients. Congress must decide how much it is worth in net costs to have an extremely low error rate. I should point out here that the only state in the country which has not flunked the system delivered only 75c on the dollar.*

Since only A+ states pass in our current system, all the other states flunk, and the sanctions label the state agencies as failures -- impairing their credibility and effectiveness in advocating within the state for concerted efforts and resources to achieve the broad AFDC goals of self-sufficiency.

* 1984 figures, which are the latest published in the HHS series: "Profiles of State Performance in the AFDC Program".

Most important, as discussed above, sanctions divert resources from our real program goals. Going back to our school analogy, a student's resource is time to study; a state's resource is money to manage. Our current sanction system is like identifying the student who's having difficulty passing and punishing him by having him spend all day washing the school buses. Not only does it not help the student; it puts him even further behind in his efforts to reach the passing grade. It does punish the student however, and it does help out the school budget a bit. Obviously, no real school would do such a thing unless it had totally lost sight of its reason for existing. If our current QC system for sanctions were actually enforced, it would be just as punitive, help out with the federal budget a bit, and make just as much sense as this school example. In reality, the student and the school both want him to succeed; likewise, Congress and each state want that state to succeed. It's important that these joint intentions aren't subverted by a budget-balancing mechanism that distorts decision-making all around.

As a last point with the school analogy, I'd like to address the bizarre notion of prospective sanctions. They appear to have no value except as another budget-balancing device, and would perhaps be akin to something like "advanced flunking". They have all the disadvantages of sanctions discussed above, but in an accelerated mode.

To summarize so far, it is of utmost importance that Congress act to correct the flawed AFDC QC system so that states can move ahead to implement its Family Support Act of 1988.

- We need a system that does not penalize states for technical errors.
- We need a passing score that identifies the extreme performers for special attention and doesn't burden the majority of states that fall in the middle.
- We need a new view of sanctions-- one that sees them as a last resort rather than as a source of federal funds.

RESPONSES TO QUESTIONS OF THE SUBCOMMITTEE ON HUMAN RESOURCES

1. How should Congress deal with the backlog of disallowances going back to fiscal year 1981?

Response:

The National Academy of Sciences and other groups have found that the current QC system is so riddled with biases and inaccuracies that the error rates it generates are unreliable as indicators of state performance. This means that those error rates cannot be the basis for deciding which states were poor performers in past years and should be subject to sanctions. At most, those error rates can serve as the starting point of an analysis as to whether sanctions are warranted. This is consistent with the approach used in industrial quality control system, which rely on error rates only as a signal that something may be wrong and that further investigation should be undertaken.

The backlog of sanctions should be handled in a two-step process. The first step is to identify the obvious cases of states that should not be sanctioned. The Moynihan bill (S. 231) provides a means for identifying these states by excluding states from sanction liability if their error rates (after certain adjustments are made) fall below a certain threshold. That threshold may be the national average or a different figure.

The second step is to provide for a case-by-case examination of states that are not automatically excluded from sanction under the Moynihan threshold. Connecticut supports the proposal advanced by states for authorizing the Departmental Appeals Board of the Department of Health and Human Services to conduct this examination and to determine whether, and to what extent, a state's QC record reflects a pattern of actual, avoidable misspending of federal dollars. The relevant factors to be considered by the Board are set out in the proposed statutory language, which is attached. This proposal would help protect against the imposition of unwarranted sanctions for past years.

2. What is a reasonable threshold above which States should be forced to pay back misspent Federal funds? Should the official error rate be the lower extreme of a statistical confidence interval? Should standard errors be published?

Response:

Connecticut supports the Moynihan bill provision that would set an error rate threshold at the national average minus one, provided that there are safeguards to ensure that only states with true error rates above this threshold will be sanctioned. The Moynihan provisions regarding the elimination of technical errors, the setting of the official error rate at the lower end of the confidence interval, and the adjustment of the error rates to take into account state demographic and program differences are one method of helping protect against inappropriate sanctions. If such protections are adopted, a threshold of the national average minus one is reasonable because it takes into account state capabilities while providing an incentive for increased improvement.

In accordance with good statistical practice, HHS should publish the standard error associated with the error rates it calculates so that Congress, the states, and the public can assess how reliable the error rates are. The National Academy of Sciences stressed the importance of the publication of this information by HHS.

3. Should so-called technical errors, those that do not have a direct effect on erroneous payments, be counted as errors for the purpose of calculating disallowances?

Response:

No, technical errors should not be counted as errors because they have no dollar cost. The counting of technical errors is one of the most arbitrary features of the current system. For example, if a newborn's social security number is missing from the case file, the whole grant is considered an overpayment even if the family meets all the eligibility tests. The comparable Medicaid and Food Stamp QC programs recognize the inappropriateness of relying on technical errors as a basis for sanctions and exclude such errors from the sanction calculation. The National Academy recommended that technical errors that do not represent misspent dollars be eliminated as a basis for sanction in the AFDC program.

4. Should States appeal directly to the Departmental Appeals Board, instead of first to the Secretary of Health and Human Services? How much time should be allotted for an administrative decision on an appeal?

Response:

Under the current system, states appeal only to the Secretary of Health and Human Services for a waiver of sanctions. HHS launched a vigorous effort to persuade the Board that it lacked authority to review the waiver decisions, and the Board ultimately adopted HHS' position. HHS has taken the position that the waiver decisions are not appealable in court either. This insulation from review has led to an abuse of the waiver process. Of the waiver requests that HHS has thus far decided (for years 1981-1984), HHS has waived only 10 of the 141 sanctions imposed. In fiscal years 1982 and 1983, no waiver requests were granted at all.

Connecticut favors permitting the Board to decide waiver issues in the first instance, as part of its overall review of a state's sanction. A reasonable deadline for an administrative decision would be six months from the date of the last submission in an appeal.

5. What factors should the Departmental Appeals Board consider in deciding an appeal? Should it consider statistical validity and reliability? Should it consider offsetting Federal savings from overspent AFDC funds, such as underspending on Food Stamps?

Response:

Although the attached proposal is specifically directed towards resolving the backlog, the list of factors set out in that proposal could also be used when the Board decides appeals prospectively. The overall standard should be whether a state's error rate reflects a pattern of actual, avoidable misspending.

With respect to the interaction between Food Stamp QC and AFDC QC, the Board should consider how AFDC error cases were handled by Food Stamp QC to ensure that a state is not penalized more than once for the same error and to ensure that errors are valued at no more than their actual cost to the federal government. This is consistent with the recommendation made by the National Academy, which was concerned that the failure of the QC system to recognize the interaction between AFDC and Food Stamp QC led to overstatement of QC errors.

6. Should the system explicitly provide for judicial review of decisions made by the Departmental Appeals Board?

Response:

The usual rule is that all administrative final decisions are subject to judicial review. Consistent with this, all Board decisions are now subject to review in federal district court. There is no reason to make a special exception for rulings by the Board in QC cases.

7. Should the Federal government charge interest on disallowances when their collection has been delayed by an appeal, if the appeal is lost?

Response:

With respect to the backlog, the issue of interest charges does not arise because there would be no sanction liability on any state until the Board determined what liability should be. As a matter of practice, only a handful of the Board's decisions on disallowances are appealed further.

With respect to future sanctions, the long-standing practice in AFDC disallowance cases has been that the right of states to appeal is not burdened by interest liability. Moreover, the Debt Collection Act of 1982 specifically confirmed that states were not to be subject to interest. We see no reason to change the existing rule.

8. Should prospective collection of potential disallowances be adopted? Should the Federal government pay interest if the State's error rate is overestimated under a prospective system?

Response:

Connecticut strongly opposes the prospective collection of potential disallowances. These sanctions would be imposed based on the error rates for prior years which are acknowledged not to be reliable. Even in a reformed system, sanctioning states based on prior period sanctions would be counterproductive because it would effectively impose a double penalty on states for their most recent error rates -- thus taking away from states the resources they need for corrective action to improve those error rates.

9. Should states be required to collect data on underpayments and negative case actions as part of the quality control samples? Should they report regularly on underpayments and negative case actions?

Response:

States currently collect data on underpayments and negative case actions, and Connecticut has no objection to continuing to do so.

10. What is the States' reaction to the Reagan Administration's proposal for a three-tiered QC liability system?

Response:

The proposed three-tiered liability system is little more than a dressed-up version of the current system. The proposed system makes some modification of the liability threshold, but does not address any of the many problems identified by the National Academy with the system for calculating error rates.

THE CURRENT Q.C. SYSTEM FOSTERS POOR PROGRAM MANAGEMENT!

. DISTORTS COST-BENEFIT DECISION MAKING
. ENCOURAGES PROGRAM EXPANSION
. DISCOURAGES PROGRAM CONTROLS/LIMITS
. DECREASES STATE RESOURCES FOR APPROPRIATE CORRECTIVE ACTION

• DISTORTS COST BENEFIT DECISION MAKING

Suppose you have a 2% Q.C. error for lack of Social Security number which projects out to $500,000 in error dollars. If you can eliminate the problem with a $100,000 corrective action, then haven't you saved $400,000?

ACTION	ERROR		SAVINGS
+$100,000	-$500,000	=	-$400,000

It appears so, but you haven't really because the $500,000 error is "FUNNY MONEY". Social Security number errors are technical errors. That is, when you correct them there are no program savings: a case may be in error for the $500 grant amount for lack of SSN's; when you obtain SSN's for the case the $500 becomes a correct payment. You still pay out the same $500 after the correction, so there are no program savings!

So what really happened in the example above?

ACTION	REDUCTION		NEW COSTS
+$100,000	- $0	=	+$100,000

We didn't reduce program costs at all, but we did increase administrative costs by $100,000. If we were running a business, this $100,000 would be considered misspent funds!

Now a smart administrator might see through this and avoid such "corrective actions". But look what happens when sanctions enter the picture:

If I'm over my target then I'll be sanctioned for the REAL FFP on that funny $500,000. Let's say 1/2 or $250,000.

ACTION	REDUCTION	SANCTION	"SAVINGS"
+$100,000	- $0	-$250,000	-(BAD PRESS) = (-$150,000)

Does it make sense to spend $100,000 to save $250,000 in sanctions (not to mention the bad press)? Of course it does; so here the administrator would take an action which we know does not make good business sense, merely to avoid the artificial, arbitrary sanction penalty. By distorting the cost-benefit decision-making process, Q.C. leads to misallocations of scarce resources and functions as a MISINFORMATION system.

Note that there are good arguments for obtaining missing social security numbers:

- Congress requires them as a factor of eligibility

- They support computer match activities

These are good arguments for SSN's, but not for putting technical errors into the Q.C. cost-benefit system.

The congressional requirement can be handled through the compliance mechanism as many others are. The computer matches are corrective actions themselves and should stand on their own cost-benefit merits as solutions to other REAL errors.

Note that Congress has deleted technical error from the Medicaid Q.C. rate.

Another problem area is excess assets. A $500 case might be ineligible because it has $50 in excess assets. The amount Q.C. counts in error is the whole grant: $500. But what happens if you correct the error? If you suspend the case until the $50 is used up, then all you save is $50, not $500. Would a $100 corrective action make sense here?

ACTION	REDUCTION	SAVINGS
+$100	~~-$500~~ -$50 =	~~-$400~~ +$50 NEW COSTS

NO. Since the real savings is only $50, then such an action would end up as $50 new costs.

So here again the Q.C. system gives misinformation which, along with sanctions, distorts cost-benefit decision-making and diverts our limited resources from areas where real savings could be made!

NOTE that Congress has corrected a similar problem in Medicaid by limiting the error amount to the recoverable dollars (here $50 rather than $500).

- ENCOURAGES PROGRAM EXPANSION

Since states share in AFDC funding (a number at 50%) there is an equally strong concern at the state level for holding down program costs.

Yet, the current Q.C. system often is a force in expanding program costs. The example just above on assets can illustrate the problem. The case with $50 excess assets caused a $500 error ($450 of which we now know is FUNNY MONEY). However, the state may be subject to a real FFP sanction on the $500. This entire problem can be eliminated by raising the state asset level by $50. Then the case will be eligible and the $500 is suddenly correct! The only catch is that now more people will be eligible for AFDC and program costs will rise. The sanction system is not fulfilling the goal of cost containment when it encourages reducing error rates at the cost of unwanted program expansion.

- DISCOURAGES PROGRAM CONTROLS/LIMITS

Strangely enough, the current Q.C. system also discourages program controls and limits. Whenever a state changes its AFDC plan by adding more stringent requirements, it leaves itself open to new Q.C. errors if the requirements aren't administered perfectly. The choice may be to forego the new limits if the Q.C. error potential seems excessive. A good example is the option to count in-kind income, which could obviously reduce program costs. Unfortunately, the process of monitoring this type of income of AFDC household members is so extremely error-prone that the potential Q.C. sanction loss will, for many states, outweigh any potential savings.

- DECREASES STATE RESOURCES FOR APPROPRIATE CORRECTIVE ACTION

Throughout the country, states are suffering from their own individual fiscal crises; program cost containment and reduction, therefore, are paramount goals everywhere. Unfortunately, states now have limited resources to improve administration, and the current Q.C. system further reduces those resources in four ways:

1) Sanctions -- FFP sanction dollars must be replaced by state dollars leaving fewer available for administrative improvements.

2) Potential sanctions and technical errors together force states to waste administration dollars trying to save FUNNY MONEY, leaving fewer available to address areas with real savings potential.

3) Potential sanctions may in themselves encourage program expansion; dollars funneled into increased program costs are not available for corrective action.

4) Potential sanctions discourage controls/limits. New controls are not put in place and the potential savings are not available for corrective action.

We need to revise the Q.C. system so that error dollars equate to potential REAL savings. We need a system that supports what everybody wants: REAL program cost containment and reduction.

- ▶REMOVE TECHNICAL ERRORS
- ▶ADJUST ASSET ERROR DOLLARS
- ▶RECONSIDER THE SANCTION APPROACH

Mr. MATSUI. Mr. Downing.

STATEMENT OF WM. REX DOWNING, PRESIDENT, NATIONAL ASSOCIATION OF HUMAN SERVICE QUALITY CONTROL DIRECTORS OF THE AMERICAN PUBLIC WELFARE ASSOCIATION, AND ADMINISTRATOR, QUALITY CONTROL DIVISION, TEXAS DEPARTMENT OF HUMAN SERVICES

Mr. DOWNING. I am Rex Downing, administrator, Quality Control Division, Texas Department of Human Services, and president of the National Association of Human Service Quality Control Directors. I am here today representing our association, which is composed of administrators responsible for the State quality control systems.

I have worked with the quality control system for the last 16 years. I will not belabor the committee with the many problems inherent in the current quality control system. I believe that there is general agreement and sufficient documentation, including those studies conducted by the General Accounting Office, and the National Academy of Sciences, in support of the need for reform. I would quickly highlight some of the major issues in my written statement.

We in the Quality Control Directors Association support a system that will only penalize the extremes of performance. We believe in a variable error rate rather than a fixed error rate, as was discussed earlier.

One of the concerns that I have with regard to a fixed error rate is that it does not take into account the accountability above State administration. The Federal agencies are responsible for issuing regulations that State administrators or State agencies must implement. The degree of complexity, the error proneness of those regulations, can cause national performance to be affected.

I believe that a fixed error rate target does not take that into consideration. I would personally prefer a target that is based on the national average with some sort of adjustment, perhaps one standard deviation below the national average.

We support a fair accountability system, one that holds state agencies accountable for areas that are within their control. Currently the quality control system does not do that. We support the removal of technical errors. We support grace periods for implementation of policy changes, and we also support a change of focus, I would hope.

The current focus of quality control does need to be changed. We are hoping for a focus on quality rather than a penalty. As was stated earlier by Mr. Greenstein, depending on what the objective is—and unfortunately the current system has created a great deal of emphasis on how to penalize States—we would hope for a focus on improved management.

By only focusing on the dollars that are lost, which is important, I am afraid we are missing the big picture. I believe what we want in a reformed quality control system is one that will focus on the process of improving performance and providing support to States to improve management.

Lastly, the system is unfair, as has been documented and discussed earlier.

I would like to recommend that the primary data collection to determine fiscal liability for States' performance, be conducted by the Federal agency. This would separate the current audit function from the State management information function.

There are other additional major improvements which are listed in my written statement.

In conclusion, I would just simply state that the question of how to resolve the quality control problem is not an easy one, but it is one that must be resolved as soon as possible. It is one that can be resolved. I believe we have an opportunity to build upon what we have learned from the current system and to create a new one that will significantly improve State agency's ability to manage the AFDC Program.

We are not only striving for good management. We are also endeavoring to provide quality service that both sustains people in severe times of need, and help them move toward self-sufficiency. At this time, States are working to implement an effective welfare reform program. A reformed QC system can only aid in the success of that endeavor.

Thank you for this opportunity to state our concerns.

Mr. MATSUI. Thank you.

[The statement of Mr. Downing follows:]

TESTIMONY OF WM. REX DOWNING, PRESIDENT,
NATIONAL ASSOCIATION OF HUMAN SERVICE QUALITY CONTROL DIRECTORS OF THE
AMERICAN PUBLIC WELFARE ASSOCIATION

Mr. Chairman and Members of the Subcommittee, thank you for the opportunity to address this hearing on AFDC Quality Control Reform. I am Rex Downing, Administrator, Quality Control Division for the Texas Department of Human Services and President of the National Association of Human Service Quality Control Directors. I am here today representing our association which is composed of administrators responsible for the state quality control systems.

I have worked with the quality control system from several perspectives over the last 16 years, as an eligibility worker, as a quality control reviewer and supervisor, as an evaluation specialist, and finally, as administrator for my state's quality control operations.

There is no question that there is a need for accountability by the federal government to ensure states are operating an efficient AFDC program. We do not oppose a reasonable sanction system. However, there are several major improvements that can be and should be made to the current system to achieve that goal as well as the goal of improved program performance.

PROBLEMS WITH THE CURRENT SYSTEM

I will not belabor the committee with the many problems inherent in current quality control system. I believe that there is general agreement and sufficient documentation including those studies conducted by the General Accounting Office and the National Academy of Sciences, in support of the need for reform.

MAJOR ELEMENTS FOR REFORM

From the perspective of state quality control staff there are several major areas for reform that will contribute significantly to improvement of states' ability to manage the AFDC program.

Effective Performance Standards

The quality control directors support an accountability system which identifies the extremes of performance. Those states that perform extremely well should be recognized and given financial incentives to maintain excellent performance. States performing poorly should be given the option of paying a financial penalty, contracting with Department of Health and Human Services (HHS) to re-invest sanction dollars in specific corrective actions to improve performance, or some combination of both. I believe that a variable target should be used instead of a fixed target with some adjustment factor (such as one standard deviation below the national average).

Establish a Fair Accountability System

In any accountability system, the measures of success must be clearly defined and achievable. The current quality control system holds state agencies accountable for errors beyond the control of the agencies. For example, clients fail to report changes that would be to their benefit such as the addition of a new eligible household member. It is clearly to the client's advantage to report these changes and yet these changes are not reported. Clients sometimes fail to report changes that would reduce their benefits. In both situations, the state agency is dependent on the client to report a change. In both situations, it is beyond the agency's control. The quality control directors support a system that would provide:

- appropriate measures of performance that can be agreed upon by the federal and state agencies; and
- accountability for only those areas within a state's control.

This reform measure alone would significantly enhance federal/state relations and improve national efforts to achieve AFDC program objectives.

Technical Errors

The current AFDC quality control system penalizes states for "technical errors". These are errors that if corrected would not result in any change to the level of benefits received by a particular client. If the focus of quality control is to identify misspent dollars, then these errors clearly should not be part of a payment error determination. HHS should monitor these errors and then report the magnitude of these errors to state agencies.

Grace Period for Policy Changes

A reformed quality control system should include a grace period whenever federal policy changes occur. Changes are naturally error prone when first implemented. For example, states are preparing to implement major changes in the AFDC program as a result of the recent enactment of the "Family Support Act of 1988". States should be allowed a reasonable period of time to implement these changes without penalty. This would contribute to a view of fairness of the system from the states' perspective.

Quality Improvement

Quality improvement encompasses a broader perspective than the current quality control system. State agencies need the tools to improve accuracy but also to improve client service. We need to be able to target our management information data collection to areas that will produce the greatest benefit.

Under the current system, state quality control staff are expected to achieve two worthy but conflicting objectives:

- to provide the Department of Health and Human Services (HHS) with data that will determine a state's fiscal liability for quality control performance; and
- to provide the state agency with useful management information in which to make program improvements.

State quality control staff are in the position of reporting information that may reduce funding for the successful operation of the AFDC program. Reduced funding would impede the ability of states to effectively manage the program.

Therefore, I recommend that HHS be responsible for data collection to determine fiscal liability for states' performance. This would allow states the flexibility to operate and target their own management information systems to address state specific issues. This recommendation should only be implemented in conjunction with other reform measures.

Additional Major Improvements

In addition to the areas that I have described, I will simply list the other areas for reform that are supported by the quality control directors.

- HHS should provide technical assistance to states with serious performance problems.
- The new system should provide a process to resolve state disagreement with federal findings in a timely manner.
- To reduce measurement error, HHS should regularly assess the level of measurement errors and the degree of bias resulting from failure to complete reviews.
- To identify the level of precision, estimates of statistical sampling errors should be routinely reported by HHS to the states.
- Samples should have equal levels of precision across states.
- The lower limit of the confidence interval should be used to measure state performance.

BACKLOG

The quality control directors support the position that for prior years' sanctions only extremely poor performance should be penalized. The system that produced the sanctions over the past years is fundamentally flawed. Collection of $1.2 billion in quality control sanctions will not improve program performance. In fact, program performance will suffer if states are forced to reduce staff or cut benefits. No one wins - - not the client, not the state agency, and not the AFDC program.

CONCLUSION

The question of how to resolve the "quality control problem" is not an easy one. But it is one that must be resolved as soon as possible. It is one that can be resolved. I believe that we have an opportunity to build upon what we have learned from the current system and to create a new one that will significantly improve state agencies' ability to manage the AFDC program. We are not only striving for good management, we are also endeavoring to provide quality service that both sustain people in severe times of need and help them move toward self sufficiency. At this time states are working to implement an effective welfare reform program. A reformed QC system can only aid in the success of that endeavor.

Thank you for the opportunity to state the concerns of the quality control directors association. I will be happy to answer any questions.

Mr. MATSUI. Leslie.

STATEMENT OF LESLIE FRYE, CHIEF, AID TO FAMILIES WITH DEPENDENT CHILDREN/FOOD STAMP POLICY IMPLEMENTATION BUREAU, CALIFORNIA DEPARTMENT OF SOCIAL SERVICES

Ms. FRYE. Good afternoon. My name is Leslie Frye. I am chief of the California State Department of Social Services, Aid to Families with Dependent Children/Food Stamp Implementation Bureau. As such, it is my responsibility to ensure that California's 58 counties operate those programs according to regulations and with as low a level of error as possible. I thank the subcommittee for this opportunity to comment on AFDC quality control and fiscal sanction issues from California's point of view.

As has been stated, these are very technical, complex issues and which makes it very difficult for all of the panel members today to be brief and to get their points across.

Instead of speaking generally, I want to address the issues California in particular sees as important. Specifically, we want to affirm the need for Congress to act this year for reform, including action to address the large sanction backlog. We want to show California's willingness to accept a balanced reform initiative as outlined in Congressman Matsui's legislation, and also to discuss previously how we feel the administration proposal falls short of dealing with the problems.

This is the third time representatives from California have testified on this subject and our position remains unchanged. The QC system drastically need reform and it is urgent and overdue. We do not oppose sanction in cases of chronic poor performance, coupled with a demonstrated unwillingness to work toward improvement. However, that isn't the way the system operates currently and as has been said before, 49 of the 50 States face some sort of sanction as a result.

The defensive exercises that we and other States engage in seriously detract from our ability to prospectively improve program performance. I began my public service career as an eligibility worker in Contra Costa County. Those years as an EW left me with a deep appreciation of the difficulties case workers face daily dealing with families in need of food, clothing, and shelter.

An eligibility worker must apply hundreds of collection regulations to the real world and do so quickly, fairly, and compassionately. The message we have given EW's over the years, despite the significant improvements in accuracy over the years, is failure. We have all failed to meet the standard set by the HHS. We believe a basic tenet of human behavior is achievable goals can spur us on to the challenge, but unrealistic goals frustrate and discourage people.

The performance standard for AFDC must be established at a level which many States have achieved. A performance standard within our reach can help us to improve our accuracy. One that has been shown year after year to be out of our reach, impossible to reach, simply serves no possible purpose. We, therefore, strongly support Representative Matsui's effort to seek reform based on the National Academy of Sciences recommendations, because we be-

lieve those recommendations will remedy the most serious flaws of the existing system.

The changes in H.R. 2243 are as follows, and we support these:

Establishing a 7-percent performance standard which does take into account State to State socioeconomic differences, using the lower limit as the determinant for levying fiscal sanctions. That figure is indisputable as a measure of performance.

We support the exclusion of technical errors when calculating a State's error rate.

We want to maintain the State's full appeal right from the Secretary of the Department of Health and Human Services through the Departmental Appeals Board and ultimately judicial review.

We support that fact that sanctions can be offset by overpayment recoveries and by child support collections.

There are two provisions in the bill which we do not welcome but we do believe are necessary for a balanced system.

The first one is expanding the quality control system to include underpayment and negative actions. While we understand the comments that have been made about a balanced system, the need for that, we do believe currently there are adequate incentives, checks, and balances, if you will, in the system to prevent States from willy-nilly imposing underpayments.

The other one is the 6-percent threshold for dealing with the past sanctions. This does leave California with a $38 million outstanding sanction. We realize we cannot eliminate all of them, but we would perhaps want to discuss that level.

We are concerned about another provision of the bill which limits overpayment collections in cases where agency errors are made. We believe this is a significant change in existing policy and would result in California's inability to collect about $72 million in overpayments every year.

We believe this change is contrary to Congress' need to inspire States to increase their collections, which have been flagging, and instead, we would like to see this bill include Federal tax intercept authority. Our State tax intercept allows us to collect approximately $4 to $6 million each year in overpayment recoveries. It has a 23-to-1 benefit to cost ratio.

We would estimate the Federal tax intercept program would allow us to collect six to nine times that amount. I didn't get to the administration but, thank you very much.

Mr. MATSUI. Thank you.

[The statement of Ms. Frye follows:]

TESTIMONY FOR THE SUBCOMMITTEE ON HUMAN RESOURCES
COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES
HEARING ON REFORM OF AFDC QUALITY CONTROL

May 8, 1989

Good afternoon Mr. Chairman, and members of the Subcommittee. My name is Leslie Frye. I am Chief of the California State Department of Social Services, Aid to Families with Dependent Children (AFDC)/Food Stamp Policy Implementation Bureau. As such it is my responsibility to ensure that California's 58 Counties operate those programs according to regulations and with as low a level of error as possible. I thank the Subcommittee for this opportunity to comment on AFDC quality control (QC) and fiscal sanction issues from California's point of view.

The topics of quality control and associated fiscal sanctions are, in addition to being very broad, quit complex and technical. This makes it difficult to be brief and still impart a full understanding of the problem. My testimony today will not address why reform is needed, since this is already well known. Instead I will address the issues listed in the hearing announcement that California sees as important. Specifically, we want to reaffirm the need for Congress to act this year for reform (including action on the large sanction backlog); to show California's willingness to accept a balanced reform initiative as outlined in Congressmen Matsui's and Downey's legislation; and to show how and why the Administration's proposal falls short of dealing with the problems.

This hearing marks the third time California has testified on this subject and our position remains unchanged. The AFDC QC and sanction system currently operating is seriously flawed and in desperate need of reform. This need is both urgent and overdue.

While California is not opposed to sanctions in cases of chronic poor performance coupled with demonstrated unwillingness to work toward improvement, the current system does not operate this way. The result is sanction liability for almost all States, except States the size of South Dakota and Nevada, which forces massive expenditures and direction of State resources toward justifying past performance rather than correcting ongoing problems. Such defensive exercises by States have seriously detracted from what could be a productive performance measurement system.

I began my public service career as an eligibility worker (EW) in Contra Costa County, California. Those years as an EW left me with a deep appreciation of the difficulties caseworkers face daily, dealing with families in need of food, clothing and shelter. An eligibility worker must apply hundreds of complex regulations to these real world situations, and do so quickly, fairly and compassionately.

It concerns me greatly that the message we give EWs, despite the significant improvements in accuracy made over the last ten years, is that they have failed. They and all of us have failed because we have not met the arbitrary performance standard of 3.0 percent.

A basic tenet of human behavior is that achievable goals challenge people while unrealistic goals frustrate and discourage them. The performance standard for AFDC must be established at a level which many States have achieved. A performance standard within our reach can help us to improve our accuracy rate. One that has been shown year after year to be impossible for most States to achieve or maintain serves no positive purpose.

For these reasons, we strongly support Representatives Matsui's and Downey's efforts to seek reform based on the National Academy of Sciences' recommendations because we believe the Academy's recommendations will remedy the most serious flaws of the existing system.

California strongly supports the changes proposed in Representatives Matsui's and Downey's bill and believes its implementation will refocus the QC/sanction system on program improvement by:

1. Establishing a 7.0 percent performance standard ceiling which takes into account State to State socioeconomic differences;

2. Requiring use of the lower limit of the error rate point estimate for levying any fiscal sanctions - a figure which is indisputable as a measure of performance;

3. Excluding technical errors when calculating a State's error rate provided the client received the correct amount of aid;

4. Maintaining State's full right of appeal, from the Secretary of the Department of Health and Human Services through the Departmental Appeals Board and ultimately judicial review;

5. Allowing sanction penalties to be offset by recouped misexpenditures and child support collections.

From California's perspective, there are two provisions we do not welcome, but we recognize as necessary to achieve a balanced bill. Those include:

1. Expanding the quality control program to include underpayments and negative actions. This imposes new performance measures that will not only increase States' workload by requiring additional monitoring, but also increases States' potential for sanction liability;

2. Setting a liability threshold of 6.0 percent to deal with the sanction backlog. Although 6.0 percent is a significant improvement, we are concerned because this still leaves California owing approximately $38.0 million. While we do not plan to relinquish any of our appeal rights, we do recognize resolution of the backlog issue is key to achieving reform and advocating total forgiveness of past sanctions is not reasonable.

I would also like to comment on a provision of the bill which California strongly opposes. This provision (on page 12) would prohibit States from collecting overpayments when the recipient was not at fault. This is a significant change in existing law and policy, and I'll explain why.

During the QC review process, each error case is categorized as either agency (welfare worker) caused or client caused. Historically, each category represents 50 percent of the cases. The proposed change could prohibit States from recouping overpayments resulting from any agency errors. This means that on up to 50 percent of the overpayment errors made throughout the nation States would be prohibited from recouping Federal, State and County aid dollars. In California alone this loss could annually total $72 million. This proposed change is contrary to Congress' need to reduce the Federal deficit and California's recent intensified efforts to enhance AFDC overpayment

collections. Instead, California would like to see a Federal law change enabling States to intercept Federal income tax refunds to offset AFDC and Food Stamp overpayments. California's State Tax Intercept Program has been operating since 1981 and is one of the most cost-effective means currently available for collecting overpayments. We estimate that a Federal tax intercept program could collect 6-9 times the amount collected through our State Tax Intercept Program, totalling $24-36 million annually in California alone.

Before closing I will briefly comment on the Administration's proposal. Although we are glad to see that the Administration has also acknowledged the need for at least some change in the QC/sanction system, their plan as outlined in the 1990 Federal budget is neither flexible or extensive enough.

Unlike the Matsui/Downey bill, the Administration proposes a stringent three-tier sanction system failing to allow for unique State differences and other reform features recommended by the Academy to establish reasonable and realistic performance standards.

Further, this plan fails to address the problem of the huge backlog of sanctions against States. Failure to do this is reason enough to reject the plan. The current price tag for these sanctions runs to the hundreds of millions of dollars. At this point collection of total sanction liabilities serves no programmatic purpose and could in fact seriously damage the ability of States to provide essential services. For California the sanction liability is estimated to be almost $250 million for 1981 through 1986. We do not ask for full forgiveness of these sanctions, only that they be recalculated on a reasonable basis. Both the Academy and the Matsui/Downey bill propose reasonable solutions.

California joins other States in urging Congress to proceed with reform this year to make the needed changes to achieve an equitable, more realistic AFDC performance measurement system and a sanction policy which promotes public confidence.

In conclusion, thank you again for this opportunity to share California's perspective and I would be happy to answer any questions you may have.

Mr. MATSUI. Ms. Orkow.

STATEMENT OF BONNIE M. ORKOW, DIRECTOR, DIVISION OF RESEARCH, EVALUATION, AND QUALITY ASSURANCE, COLORADO DEPARTMENT OF SOCIAL SERVICES, AND VICE PRESIDENT, NATIONAL ASSOCIATION OF HUMAN SERVICE QUALITY CONTROL DIRECTORS OF THE AMERICAN PUBLIC WELFARE ASSOCIATION

Ms. ORKOW. My name is Bonnie Orkow, and I am director of quality assurance in Colorado and also vice president of the National Association of Human Service Quality Control Directors.

The current quality control system penalizes honesty, does not reward excellence in management, and is inequitable. Allow me to tell you some short stories that will bring home my point:

Quality control reviewers audit county records and the reviewers do find errors. When they find errors at the county level they bring those errors back to the State and the State program staff reviews those errors, and try to persuade the quality control reviewers to reverse the findings. Program staff use every possible policy nuance to convinced the quality control reviewers to reverse the findings.

Then the Federal staff comes along and they look over the State's work. When Federal staff find an error, they report it to the State. Suddenly the State quality control reviewers and the program staff are on the same side of the fence, and they both work together to try to reverse the Federal findings. So, what you have here is a cat and mouse game. It is certainly not a game that promotes honesty in the system.

Allow me to tell you another story about management excellence. This story is a Colorado specific story. Colorado has always been committed to a low error rate. In 1978 when the Government first declared that they were going to look at determining an overall error rate that was a national system, Colorado's error rate stood at 4.2 percent. That was almost at tolerance, because at that point, the error rate nationally was to be 4 percent.

Despite that good performance Colorado started several significant programs to lower its error rate even further. One of those special projects was what we called a SEED project. It was called State Evaluation of Eligibility Determination and it ran from 1982 to 1986. Colorado almost doubled quality control review staff during those years in order to run that program. Operating funds came from our State general fund. The program was supported by the State legislature and by the Governor.

What the SEED workers did was to go out to every single county in Colorado and review records of each county to try to find the errors and also set up a system in each county once they found the errors to correct the errors in those counties. Corrective action was mandated in every county where errors were found, even though such "errors" were sanctionable at that point.

We also took over State administration of Colorado's largest county, Denver County, for 1 year. We made significant changes that year in Denver County. We set up videotapes in the waiting room so that clients applying for services heard the same messages

regarding what services were available and what rules and regulations those clients had to follow in order to meet the eligibility criteria. Every error case was reviewed by State staff administering the program. County staff had to set up corrective action measures for all those errors. Again, the corrective action measures were overseen by State staff.

We also undertook some other special projects that were more centralized toward food stamps. You understand that even though it was centered on the Food Stamp Program, you get a synergistic effect here because the eligibility workers who determine food stamp eligibility also determines AFDC eligibility.

Today, Colorado's AFDC error rate is 1.8 percent. But because we weren't able to achieve such a low error rate earlier, we in Colorado are liable for $6.1 million in sanctions. That translates into 1 year's worth of AFDC administrative dollars in Colorado. If these dollars are collected, we are not going to be able to totally implement our welfare reform project that was mandated by the Family Security Act last year, because the same staff that administer our AFDC Program also would be the staff to implement our welfare reform initiative.

I have other stories to tell you. My time is up. Let me assure you Colorado's experiences with this program is not unique. The system needs reform.

Thank you very much.

Mr. MATSUI. Thank you very much.

[The statement of Ms. Orkow follows:]

TESTIMONY OF BONNIE M. ORKOW
DIRECTOR, DIVISION OF RESEARCH, EVALUATION, AND QUALITY ASSURANCE
and VICE PRESIDENT
NATIONAL ASSOCIATION OF HUMAN SERVICE QUALITY CONTROL DIRECTORS

Mr. Chairman, and members of the Subcommittee , I am pleased to have the privilege of speaking before you today during this hearing on AFDC Quality Control Reform. My name is Bonnie Orkow. I am the Director of Quality Control for Colorado, and I am also vice-president of the National Association of Human Service Quality Control Directors. My goal today is to speak to you as an administrator of the current system and as a representative of other state quality control directors who could not be here to speak before you today. I am new to quality control. I did not come up through the ranks as many of my colleagues did. I was introduced two years ago to the quality control system, and I came in as the boss. But what I saw two years ago, I did not like. And so I have become very involved with the system in hopes of making a difference.

The Problem With The Current System

What we currently have is a system that penalizes honesty, does not reward excellence in management, and is inequitable. My understanding is that no one meant it to be that way. But the bottom line now is we have a system that does not work effectively. We have quality control reviewers who audit county records and find errors (i.e., clients who are getting welfare benefits who are not entitled to them). When reviewers find errors at the county level, the state program staff, who administer the AFDC program, use every possible policy nuance to reverse that finding. Then the federal staff come along and look over the state's work. When they find an error and report it to the state, the state reviewers and the state AFDC program staff suddenly are on the same side and both use every angle they can find to make the federal staff not cite the error. The game is about money and power. States are sanctioned for errors. And states are now faced with a $2.1 billion dollar debt which the federal staff has written into their budget proposal, and promised to collect. Congress doesn't want to back down from collecting that money because there is a huge national deficit, and because leaders in Washington are not convinced that states have done their job as well as they might in order to prevent errors. As Mr. Rex Downing has already said, <u>the focus of the present system is negative</u>.

Colorado's Story of Management Commitment to Quality Control

Allow me to tell you a story. This story is about Colorado. Colorado has always been committed to a low error rate. With the amendments to the Social Security Act in 1969, assistance payments staff were separated from social services staff. States assistance payment staff began taking clients' declaration of income and were not mandated to check out the accuracy of that data. Some states became less concerned about errors because there was no way to track those errors. Federal advisors felt the "declaration system" would be less expensive to administer. But the error rate went up over the years as clients realized their declarations of income were not checked. Remember, that was a decision made in Washington. Colorado still monitored its error rate, so that our error rate was never high. But then the federal rules changed and a system was set in place to penalize states who did not monitor their eligibility errors. Please be aware: states achieved their greatest reduction of errors <u>before</u> the imposition of federal penalties in 1981. The base year for establishing a sanction system was 1978. Colorado's error rate then was 4.2%. The tolerance level above which states were financially penalized was 4%. So Colorado was almost at tolerance. Many states error rates were between 10-20%. Since 1978, Colorado has had only two years where its error rate increased over the prior year. Both were due to massive government changes, and even though errors were exempted for a period of time after those massive government changes, we believe the learning curve for county technicians was slower than the grace period allowed for learning the new system.

Colorado has had three special projects to lower its error rates:

1) The SEED project (State Evaluation of Eligibility Determination), which ran from 1982-86, involved state staff looking at case records in every county and in every program and taking corrective action toward counties where errors were found.

2) State administration of Colorado's largest county, Denver County, for one year ('82-'83). Significant changes were made in Denver county that year. Video tapes were set up in waiting rooms so clients applying for services heard the same messages regarding what services were available and what rules and regulations they had to follow. Every error case was reviewed by state staff administering the program, and county staff had to come up with ways to correct these problems. Corrective action measures were overseen by the State.

3) State administration of Denver Food Stamp Offices from 1983 to the present where the error rate in that program was over 15% and is now close to the tolerance level for the food stamp program.

Today, Colorado's AFDC error rate is 1.8%. But because we weren't able to achieve the arbitrarily set tolerance level in past years, despite special efforts, Colorado is liable for $6.1 million. This translates into one year's worth of federal dollars to run our entire AFDC program . If these dollars are taken from us, we will not have the administrative dollars to pay the county technicians who process client applications. Colorado is using present AFDC administrative dollars to start up a self-sufficiency program which is mandated under the recently passed Family Security Act of 1988. If our AFDC administrative dollars are used to pay back the federal government, Colorado's efforts at start-up on self-sufficiency will not be possible. As Mr. Rex Downing has already said, the system measures only payment errors, ignoring other major program objectives.

Minnesota's Experience With Federal Controls Over Quality Assurance

Then there is the Minnesota story. This state experienced a keypunch error as they transmitted all their review data to Washington. This was the only key punch error in the 2400 cases that were typed in to Washington. The error wasn't caught because this incident preceded the time period when the system had an edit check on such keypunch errors. There was agreement that the error wasn't an eligibility error, but a keypunch error. But it didn't matter. The federal government, because of rules that were on the books, used the error when calculating the regression formula. So Minnesota received a sanction for that year because of that one error. Reversal of that typographical error would have put Minnesota under the tolerance and saved the state $150,000, all caused by a typo. The real dollar loss can be calculated by considering the state staff time and resources necessary to write waiver requests and possibly to fight this case in court. The same year this all occurred, Family Support Administration gave Minnesota their award for State Excellence in Program Administration. (contact John Petroborg for additional details). Enough stories. But be assured that these stories are not unique. California staff are here today to tell you their experiences. If this hearing were any longer, you could possibly learn about other stories which demonstrate state frustration with the current system.

Major Elements for Reform

I have spoken with many state administrators. The following lists their primary recommendation:

1) Eliminate the arbitrary 3% tolerance level. Establish a tolerance level based on the national average error rate plus one standard deviation using statistically valid data from the immediately preceding fiscal year. (We estimate that 86% of states would not be liable for sanctions under this system, but those who are outliers would still be responsible to pay for their errors.)

2) Instead of demanding that states pay back all past sanctions, we suggest that the lower bound of the confidence interval rather than the point estimate be used for each of the prior years; and that all past technical errors be eliminated from those calculations.

3) Establish a one-tiered Q.C. system

4) Expect Regional Offices to provide technical assistance for states who: (A) ask for such assistance, or (B) are outliers where state corrective action measures are indicated.

5) Hold states harmless for errors caused by legislative changes in eligibility criteria occurring within one year after the effective date of those changes.

6) Hold states harmless for errors caused by changes in federal administrative policy for 120 days beginning on the effective date of such changes or mandate that all proposed Federal Administrative changes be published and State input sought 60 days before being finalized.

7) Settle error rate disputes between federal and state staff at the lowest levels, i.e., appeals should go to Health and Human Services first for resolution, followed by judicial review, if agreement can not be reached.

8) Review against an error rate determination plan that provides for measurement of errors against State practices as outlined in State regulations and policy in order to establish criteria by which States will be held accountable.

Conclusion

The Quality Control system is almost 20 years old. Problems have been recognized for much of that time. Congress itself recognized major problems with the system and so it mandated the National Academy of Sciences study. Congress has three times imposed a moratorium on the collection of the sanctions. You may choose to extend that moratorium again. But the longer states go without a resolution, the greater the likelihood that their resources will be spent on litigation activities and the less likely it is that their ultimate energies can be focused on moving their clients from a system of penalties to a system of self-sufficiency. Thank you for allowing me to speak with you. I would be pleased to respond if there are any questions.

APPENDIX A

List of Select States Who Are Liable for Financial Losses to Their AFDC Program

States	State Losses if Sanctions Collected
Tennessee	$4,593,000
New York	$226,358,000
Ohio	$74,677,000
California	$247,807,000
Connecticut	$4,636,000
Texas	$16,445,000
Pennsylvania	$74,105,000
Florida	$22,123,000
Colorado	$6,471,000

Mr. MATSUI. Mrs. Johnson.

Mrs. JOHNSON. Thank you for your frontline testimony here. I just have one question.

To what degree could we simplify the administration of this program by making the eligibility criteria for Medicaid, food stamps, and AFDC similar and less complex? Clearly, they can't be 100 percent identical, but could we be making things a lot easier and reducing your administrative costs?

Ms. FRYE. I think we certainly could, particularly in areas that have to do with definitions of income. These seem to be assured on the front line level.

For example, what kind of income is included in AFDC and included in food stamps. I appreciate the fact that some of the factors as far as which family members are eligible for inclusion, or exclusion really shape the basic thrust of the program, but once we move beyond that, the detail level of the kind of things that a worker has to keep in his or her mind is the fact that two types of income are treated differently, one type of property is treated differently in two programs really ought to be able to be worked out.

I don't know why that hasn't happened sooner, but it is a cry we hear constantly from our front line staff.

Mrs. JOHNSON. Thank you.

Others.

Ms. ORKOW. I concur with what has already been said.

Let me use an analogy, if I might. Grocery store chains in the last decade or so found that a significant number of errors with checkout clerks occur—I think it was 40 to 60 percent—people who went through the lines in grocery stores were being charged incorrectly because the cost of the groceries was changing every couple of days, and clerks couldn't remember all the current prices.

Many stores now have a computerized system and that, to a large extent, has eliminated all the errors in the grocery line.

We could do the same thing for the AFDC and food stamp eligibility process. In Colorado we are looking at what we call a "smart system," which puts all the eligibility rules and regulations on a computer and calculates eligibility determinations by machine. The eligibility technicians could then concentrate on teaching clients how to get on the JOBS program and how to access some of the services that are available in the community, rather than worrying about all of those fine points of eligibility rules and regulations.

Ms. DAY. I would agree. If we could make them more uniform not only would it reduce error, but it would prevent more error from coming up. In Connecticut we are a little bit ahead of Colorado and are actually getting started with our new automated eligibility system.

To do that, we have had to put all of the rules into our computer system and we have had to change what our workers do. Previously they were specialized. Now, they're becoming generalists, and to know all these rules is just mind boggling. We think that part of our increase in error rate is due to the fact that there is so much to know. If we can make it more uniform it would work wonders in improving that.

Ms. BLONG. I think we could all agree obviously if it was uniform it would be simpler to administer. I don't think the question of

whether or not one can reach uniformity is simple. There are very different standards in some of the programs reflecting very deeply held views of those people who shaped the statute, and I think a critical factor in any discussion of simplicity is what directions do the procedures move in, and what choices are made.

Mrs. JOHNSON. I appreciate that and any concrete suggestions you have for us would be appreciated. It is clear we shouldn't pass up this opportunity to improve the overall quality control system since some steps have been made in other bills in recent years.

Thank you very much.

Thank you, Mr. Chairman.

Mr. MATSUI. Thank you, Nancy.

I just have one comment to make, Leslie. In terms of the concern you have—and certainly we want to work with you—I am sure our office and certainly the subcommittee—on any proposals any of you might have in improving the process, and improving my legislation, improving the whole thrust of whatever legislation we eventually come up with.

But in terms of that provision about States which collect overpayments where the recipient wasn't involved, where we actually forgive the recipient for any overpayment, if you look at the legislation which is on page 12, we have two conditions, and it is in the conjunctive, not the disjunctive. It basically means payments would be waived if the individual was without fault in connection with an overpayment and any adjustment or recovery of the overpayment would defeat the purpose of this part of the act or be against equity in good conscience.

So really, it is discretionary with the agency involved. Now, certainly if you have some language that could clarify that further to make sure that it is a discretionary action by agency, we certainly would like to have that, because I think what you say is well taken. We don't want to put a position in there where if a person has assets we couldn't collect from that person.

Ms. FRYE. I appreciate that, and we would be happy to discuss that further. I think at this juncture, we feel that language is pretty imprecise and very wide open to individual interpretation, which would in effect lead to a considerable reduction in our ability to recover misspent payments.

Mr. MATSUI. I appreciate that.

Ms. BLONG. Mr. Matsui, if I could comment on that point, I think it is important to recognize that as a standard that has been used in the title II Social Security Program since its inception, a standard that is now used in the SSI Program, to which the Federal Government binds itself for administration of its own program.

Mr. MATSUI. We will look at it from the perspective of both of you and make sure whatever attempt we really want to carry out will be clear in the language.

I have been through these issues on quality control the past 4 years. This is the fifth hearing I have attended. I have exhausted myself on questions. So we look forward to working with you again, and thank you for your testimony.

[Whereupon, at 3:25 p.m., the hearing was adjourned.]

[Submission for the record follows:]

STATEMENT OF DR. KERMIT R. McMURRY, STATE DIRECTOR,
NEBRASKA DEPARTMENT OF SOCIAL SERVICES

With the moratorium on collection of Aid to Families with Dependent Children (AFDC) quality control sanctions scheduled to expire June 30, 1989, the State of Nebraska faces penalties in excess of $4.9 million for fiscal years 1981 through 1984. Additional sanctions are expected for fiscal years 1985 through 1988. Nebraska is not alone in this issue; currently all states but one are sanctionable for quality control penalties in the AFDC program.

These sanctions pose a menacing threat to our ability to deliver services to low income families. With the pending sanctions the states may be forced to increase administrative costs with little or no evidence that such expenditures will be cost-effective. This will have an immediate and significant impact on the ability of states to finance human service programs.

The sanctions are based on a system which has been questioned by Congress, criticized by the National Academy of Sciences, faulted by the General Accounting Office and litigated by the states. It is my hope that Congress will act quickly to make needed changes in view of the flaws identified in the present quality control system.

We lend our support to the views of the National Governor's Association and the National Council of State Administrators in support for reform of the Quality Control system.

Two important issues must be addressed. First, a resolution must occur regarding the backlog of sanctions calculated under prior law. The study commissioned by Congress from the National Academy of Sciences has confirmed that the federal error rates on which these sanctions are based demonstrate little relationship to whether a state has responsibly managed the distribution of funds to assistance recipients. Second, there is a critical need for reform of the system as recently proposed in S. 231 (introduced by Senator Moynihan and soon to be introduced by Representative Matsui).

How should Congress deal with the backlog of disallowances going back to fiscal year 1981?

Nebraska feels that the Departmental Appeals Board of the Family Support Administration should examine the presentation of each state that does not qualify for an exclusion from sanctions under proposed S. 231 and the similar Matsui House bill. The Board should determine whether sanctions are warranted for the state and the appropriate sanction amount. The determination should be based on an inquiry of whether, and to what extent, a state's quality control error rate reflects a pattern of actual, avoidable misspending of federal dollars. The inquiry should follow the standard used by the National Academy of Sciences; i.e., states should be held accountable only to rules that are known in advance and for procedures over which they have control.

The relevant factors to be considered by the Board must include:

1. Whether the state's error rate is sufficiently statistically reliable for a conclusion that the state exceeded the tolerance level or whether the state's penalty is upwardly biased;

2. Whether the errors for which the state was cited in fact represented misspending of benefit dollars;

3. Whether the errors for which the state was cited could have been avoided by the state agency by cost-efficient means that would not have interfered with program purposes;

4. Whether the state's error rate is based on errors that are also reflected in the state's error rate for another welfare program or whether the error rate is based on monies that have been previously recouped by the federal government;

5. Whether the state's error rate history is consistent with the error rate for the period in question;

6. Whether the error rate was affected by factors beyond the state's control, such as caseload growth, caseload composition, program changes, strikes, or natural disasters; and

7. Whether the state's record with respect to corrective action demonstrates a concerted effort to reduce errors.

If the Board determines that a sanction is warranted, the state should be allowed to seek judicial review of the Board's decision. No sanction should be collected until all steps are completed.

If a sanction is ultimately imposed, a state should be allowed to fulfill its sanction obligation by investing at least one-half of the sanction amount in corrective actions to reduce errors and enhance program management.

REVISION TO FUTURE SYSTEM

Both Federal and State government are responsible for administration of the AFDC program, therefore both should be held accountable for efficient management of this program. Because of the flawed QC process, a reformed system must be enacted.

In the future, acceptable measures of performance should be based on reasonable statistical estimates designed to shift the margin of error appropriately, i.e., use of the lower bound of the confidence interval in lieu of the point estimate in calculating payment accuracy rates. Also, a fair measure of performance must consider significant demographic and program variations within and across the states.

A reasonable threshold should be established based on a national average error rate for AFDC underpayments and overpayments for the preceding fiscal year minus one. The tolerance level should be derived from actual error rates, but still require incremental improvement over the national average error rate for the previous year. The error rate tolerance level should be adjusted to account for varying State organizational and administrative differences which affect administration of the AFDC program.

Just as purely technical errors and errors due to recent Federal changes in eligibility criteria or administration methods should be disregarded from the backlog sanctions, they should also be eliminated from the calculation of future error rates.

Technical errors are errors in procedure that do not result in incorrect payments, such as missing Social Security numbers, monthly reporting errors, informational and work program registration errors. Elimination of technical errors alone would bring Nebraska into compliance within the Federal tolerance levels for several of the years in question. For example, in fiscal year 1983, 13.1% of the Nebraska errors were the result of a single technical error, work program registrations. In fiscal year 1984, one-third of the total sanction amount is due to technical errors. We feel strongly that states should only be penalized for actual misspent dollars. Technical errors should not be tied to fiscal penalties.

A second level review of state Q.C. files is performed by federal reviewers. Their findings also affect the State error rate. We believe states should not be penalized for error based on information unavailable at the time of the state review, yet available at the time of the federal review.

The factors to be considered before imposing a state sanction should be based on moving toward a quality improvement system based on a broader assessment of state performance. State sanctions should be reduced by the federal share of overpayments collected by the State from AFDC families. Child support collected should also be taken into consideration. Presently, subsequent past due child support collections and repayments by families are not credited to the state's error rate on overpayments. Further, a family eligible for both AFDC and Food Stamps who receives an AFDC overpayment has probably received a Food Stamp underpayment. While this is not a dollar for dollar exchange, only the net overpayment from the two programs should be considered.

Federal support is needed to minimize the impact of federal program and policy changes on state performance. Special attention must be given to simplifying, and coordinating the three diverse Federal programs--AFDC, Medicaid and Food Programs. Federal support in the proposed final regulations containing standards has been lacking.

Nebraska feels that it is not appropriate for the Federal government to charge interest on the pending disallowances, as the delays in the assessment and appeal process have not been caused by the state. Prospective collection of the disallowances further hampers the appeal process.

Currently the Quality Control System considers only overpayments and ineligibles, the system should be expanded to include underpayments and inappropriate denials. Since improper authorizations of ineligible households are included in error rates, improper denials and terminations of eligible households should be included to give the quality control balance between errors in granting benefits to ineligibles, and errors denying help to the needy.

In conclusion, it is appropriate for us to place our attention on more than "are we accountable" to include "do we have a valid system for evaluation of quality". We ask your active support now for federal legislative relief. Nebraska feels that the sanction figures do not accurately portray the high level of performance we are actually achieving.

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